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Supreme Court of the United States

OCTOBER TERM, 1956.

No. 560

ISRAEL BALANOVSKI, SAMUEL BERNARDO HORENSTEIN, COMPANIA ARGENTINA DE INTERCAMBIO COMERCIAL, I. BALANOVSKI & CIA. (sometimes called "CADIC"), a co-partnership,

Petitioners,

v.

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1956.

No. .

ISRAEL BALANOVSKI, SAMUEL BERNARDO HORENSTEIN, COMPANIA ARGENTINA DE INTERCAMBIO COMERCIAL, I. BALANOVSKI & CIA. (sometimes called "CADIC"), a co-partnership,

Petitioners,

against

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

Petitioners respectfully pray that a writ of certiorari be issued to review the judgment of the United States Court of Appeals for the Second Circuit, entered August 14, 1956, affirming in part and reversing in part a decision of the United States District Court for the Southern District of New York entered on June 23, 1955.

Citations to Opinions Below.

The opinion of the District Court, printed in Petitioners' Appendix (Pets.' App. 6-26)* is reported at 131 F. Supp. 898. The opinion of the Circuit Court of Appeals is printed in Appendix B hereto, *infra*, pp. 4a-19a, is not as yet officially reported but will be found in 4 P-H Fed. 1956, Par. 72,886.

Jurisdiction.

The judgment of the Court of Appeals was entered on August 14, 1956. Jurisdiction of this Court is invoked under Title 28 U. S. C., Sec. 1254(1).

Questions Presented.

1. Is personal jurisdiction acquired by the District Court by reason of a non-resident alien's appearance and interposition of a defense on the merits in that Court?

2. Are non-resident aliens subject to tax on their income from sales to foreign customers under contracts executed abroad, because letters of credit are employed which provide for the delivery of documents of title to a correspondent bank in the United States?

3. Do the activities of a non-resident alien in purchasing merchandise within the United States and shipping the same to foreign customers constitute doing business within the United States?

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* Where "Pets.' App." is referred to herein it means "Appellants' Appendix" filed in the Court of Appeals; similarly, "Gov. App." means "Appellee's Appendix".

4. Can the Commissioner of Internal Revenue revoke with retroactive effect a published ruling, consistently followed by him for 17 years, upon which the petitioners had relied?

Statutes and Regulations Involved.

This case involves the following statutes and regulations:

Internal Revenue Code of 1939: Sec. 119(e), Sec. 212(a), Sec. 3791(b).

Treasury Regulations 111: Sec. 29.119-8, Sec. 29.212-1(a).

Federal Rules of Procedure: Rule 4(d)(1), 12(b).

They are set forth in Appendix A, *infra*, pp. 1a-3a.

Statement of the Case.

The petitioners, Balanovski and Horenstein, are nonresident aliens and members of an Argentine partnership, Compania Argentina de Intercambio Comercial (hereafter referred to as "CADIC"). On December 20, 1946, Balanovski, as CADIC's representative, came to the United States for the sole purpose of purchasing automotive equipment which the partnership had contracted or proposed to sell to the Argentine Government's purchasing agency, Instituto Argentino de Promocion del Intercambio (hereafter referred to as "IAPI") (Pets.' App. 46 [Stip. Pars. 19, 20]).

Balanovski remained in the United States for 10 months, acting as CADIC's purchasing agent, locating suitable merchandise, negotiating purchase prices and arranging for shipment of such merchandise to Argentina. All of this

merchandise was sold by CADIC to a single customer, IAPI, under contracts negotiated and executed in Argentina. In fact, Balanovski did not order material from a supplier in the United States until he had an order and letter of credit from IAPI (Gov. App. 13a).

When IAPI had contracted to purchase a particular shipment from CADIC, it would cause a letter of credit to be opened in favor of CADIC or Balanovski with a New York bank. Under the terms of such a letter of credit, payment was to be made against delivery of the usual documents of title, with invoices, licenses, inspection certificates, etc., to the goods described therein. Balanovski would assign a portion of the letter equal to CADIC's purchase price to the United States supplier of the goods, who would receive his payment upon delivery to the bank of his invoices, warehouse receipts, etc. Subsequently, Balanovski would withdraw the balance of the credit upon transmitting to the bank CADIC's invoices to IAPI and the various shipping documents required thereunder. In addition to these payments, Balanovski also received from the United States suppliers discounts for quantity purchases (Pets.' App. 50 [Stip. Par. 34]).

Balanovski negotiated approximately half of CADIC's purchases in 1947, the balance being completed for CADIC's account by other purchasing agents, namely, Trading and Shipping, Inc., a New York corporation, and Mayorga Hermanos, an Argentine partnership. The method of operation was substantially the same whoever negotiated the purchases in the United States (Pets.' App. 50-1 [Stip. Par. 35, 36]).

In October of 1947, Balanovski returned to Argentina and has never since been in the United States. Horenstein was never at any time present here (Gov. App. 63a).

On March 12, 1948, the Commissioner of Internal Revenue issued an assessment and notice of demand against Balanovski for payment of 1947 income taxes, and served the same upon one Alice Devine, his purported agent. Additional assessments were thereafter issued against both Balanovski and Horenstein, aggregating, with interest, more than $8,000,000.00 (Pets.' App. 45 [Stip. Pars. 14-15]).

On April 6, 1949, the present action was commenced by the Government to foreclose a Federal tax lien on partnership funds on deposit in two New York banks and to obtain judgments against Balanovski and Horenstein in the sums (as set forth in the last amended complaint) of $6,722,625.54 and $1,672,209.90, respectively (Pets.' App. 30). Service of the summons and complaint on Balanovski and Horenstein was effected in Buenos Aires, Argentina; Miss Devine, the purported agent of Balanovski, was personally served in New York (Pets.' App. 70 [Stip. Par. 3]).

Following the service of the complaint, as aforesaid, the respondent served and filed four amended complaints in this action. The petitioners filed answers to each of these complaints and in each answer challenged the Court's jurisdiction over their persons or their property and, at the same time, pleaded their defenses to the merits (Pets.' App. 31-33).

Pursuant to notice, depositions were taken of defendant Israel Balanovski on April 30, 1953 (Pets.' App. 71) of Alice Devine on October 30, 1953, and of William Alfred Harloe on November 5, 1953 (Gov. App. 49a, 72a).

Thereafter, on November 30, 1954, the case was tried before the Court without a jury, Judge Edmund L. Palmieri. The defendants appeared and participated in the said trial although they repeated their challenge to the Court's jurisdiction at the opening thereof (Pets.' App. 6, 41).

The District Court held that it had personal jurisdiction over the petitioners because of their appearance in defense of the action and that a lien upon CADIC's bank accounts in the United States provided the Court with *in rem* jurisdiction over the individual partners. The Court determined, further, that CADIC's purchasing activities did not constitute conducting a trade or business in the United States, that the sales made by CADIC to IAPI were consummated in Argentina where the substance of the transaction occurred, and that the income from such sales was not from sources within the United States. However, it concluded that the quantity discounts paid by the United States suppliers represented separate income to Balanvoski and Horenstein from sources within the United States which was taxable to them here (Pets.' App. 12-16).

The District Court entered a judgment against the petitioners in the sum of $999,709.62 and the petitioners appealed therefrom to the Court of Appeals for the Second Circuit. The respondent cross-appealed because of the District Court's failure to direct the entry of personal judgments against Balanovski and Horenstein in the sums of $5,050,415.64 and $1,672,209.90, respectively, with interest thereon.

It was the decision of the Court of Appeals that, since the petitioners appeared and defended on the merits, the District Court had acquired power to render a judgment *in personam* conditional only upon the validity of the original *quasi-in-rem* jurisdiction. Upon the substantive issues, the Court of Appeals held that the District Court erred in deciding that CADIC's activities in the United States were not equivalent to conducting a trade or business and also in holding that the sales to IAPI were not consummated here. Therefore, on the petitioners' appeal

it affirmed the decision below and, on the respondent's appeal, it reversed the judgment of the District Court (App. C, *infra*, pp. 18a-19a). Upon remand to the District Court, judgment was entered against the petitioners in the amounts of $5,878,923.53 and $1,928,877.31 respectively.

Reasons for Granting the Writ.

1. The decision below upon the question of jurisdiction *in personam* is in direct conflict with the decision of the Court of Appeals for the Sixth Circuit in *Salmon Falls Mfg. Co.* v. *Midland Tire and Rubber Co.*, 285 F. 214, with the decision of the Court of Appeals for the Fourth Circuit in *McQuillen* v. *National Cash Register Co.*, 112 F. 2d 887, cert. den. 311 U. S. 695, rehearing den. 311 U. S. 729, and with the decision of the Court of Appeals for the Ninth Circuit in *Fahey* v. *O'Melveny, et al.*, 200 F. 2d 420. This conflict *was conceded in the Court's decision below.*

2. This case presents important questions of Federal tax law which have not been, but should be, specifically settled by this court.

I.

There is a direct conflict among the circuits on the question of jurisdiction.

The Court below decided that despite the absence of personal service of process the District Court had acquired personal jurisdiction over the petitioners by reason of their appearance and presentation of a defense on the merits. It acknowledged, however, that its position was in conflict with the views of various other Courts of Appeals, stating:

"While this point has provoked some conflict, we regard the cases so agreeing as stating the better rule. *Anderson* v. *Benson*, D. C. Neb., 117 F. Supp. 765; *Grant* v. *Kellogg Co.*, D. C. S. D. N. Y., 3 F. R. D. 229; *Bede Steam Shipping Co.* v. *New York Trust Co.*, D. C. S. D. N. Y., 54 F. 2d 658; *Campbell* v. *Murdock*, D. C. N. D. Ohio, 90 F. Supp. 297; 2 Moore's Federal Practice par. 12.13 (2d Ed. 1948). For the contrary view see *Salmon Falls Mfg. Co.* v. *Midland Tire & Rubber Co.*, 6 Cir., 285 F. 214; *McQuillen* v. *National Cash Register Co.*, 4 Cir., 112 F. 2d 877, certiorari denied 311 U. S. 695, rehearing denied 211 U. S. 729; *Proctor* v. *The Sagamore Big Game Club*, D. C. W. D. Pa., 128 F. Supp. 885; cf. *Fahey* v. *O'Melveny & Myers*, 9 Cir., 200 F. 2d 420."

Conflict with Salmon Falls Mfg. Co.* v. *Midland Tire & Rubber Co.

The defendant in *Salmon Falls Mfg. Co.* v. *Midland Tire & Rubber Co.*, 285 Fed. 214 (CCA 6, 1922), filed an answer to the complaint in which, in addition to denying the merit of the plaintiff's action, it challenged the jurisdiction of the Court. At the opening of the trial the defendant moved the Court to limit the scope of the hearing to the value of the property attached.

The Court reserved its decision on this motion and proceeded with the trial. As in the present case, the defendant participated in the trial upon the merits. The District Court decided in favor of the plaintiff and rendered a personal judgment against the defendant for the full amount claimed in the complaint.

The Sixth Circuit Court of Appeals reversed and held that the District Court's jurisdiction was limited to the property under attachment. It further held that the defendant did not waive its objection to personal jurisdiction by participating in the trial after its ineffectual attempt to

limit recovery, so long as it persisted in its protests against a personal judgment. The Court pointed out that if the rule were otherwise, personal jurisdiction could be avoided only by surrendering a defense to a recovery to be satisfied only out of the attached property.

In the present case the Court below took the position that a defendant could challenge the Court's jurisdiction along with his other defenses (as provided in F. R. 12(b)) but that if the jurisdictional defense is held invalid, he has exposed himself to a personal judgment for the full amount in issue. This construction is squarely in opposition to the rule established by the Sixth Circuit in *Salmon Falls Mfg. Co.*

Conflict with McQuillen* v. *National Cash Register Co.

A motion was filed by the defendant in *McQuillen* v. *National Cash Register Co.*, 112 F. 2d 877 (CCA 4, 1940) for an order limiting the jurisdiction of the District Court. This motion was granted and the Court below ordered all matter stricken from the amended complaint which sounded *in personam* and limited the jurisdiction of the Court to such claims as were claims *in rem* against the stock of the defendant corporation.

In affirming the decision below, the Fourth Circuit held that litigants should be permitted to make special appearances for the purpose of attempting to limit the Court's jurisdiction and that "it would indeed be an unfair attitude were the federal courts, under such circumstances, too prone to treat a special appearance as a general appearance". The Court recognized that some conflict on this subject existed. It noted that the decision in *Bede Steam Shipping Co.* v. *New York Trust Co.*, D. C. S. D. N. Y., 54 F. 2d 658 (the decision relied upon by the Court below in the present

case) contained language opposed to its views but the Court flatly declined to follow such language.[1]

Conflict with Fahey v. O'Melveny & Myers

Although the question of jurisdiction was not essential to the result in *Fahey* v. *O'Melveny & Myers*, 200 F. 2d 420 (CCA 9th 1952), the Court of Appeals for the Ninth Circuit observed parenthetically that it was its view that a jurisdictional challenge asserted by the defendant therein had been effectively preserved and in a footnote at page 451 the Court stated:

> "The effectiveness of this sort of challenge to the jurisdiction is not lost, nor is not waived by coupling it (as was done here) with a defense on the merits. It is basic under Rule 12(b) of the Federal Rules of Civil Procedure, 28 USCA, that a challenge to the jurisdiction of the court may be joined with a defense on the merits without any waiver resulting. See *Orange Theatre Corp.* v. *Rayherstz Amusement Corp.*, 3 Cir., 1944, 139 F. 2d 871, 874; *Gerher* v. *Fruchter*, 2 Cir., 1945, 147 F. 2d 120; *Blank* v. *Bitker*, 7 Cir. 135 F. 2d 962; *Devine* v. *Griffenhogen*, D. C. 31 F. Supp. 624, 2 Moore's Federal Practice, p. 2200, 2nd Ed."

Conflicts with other Courts of Appeals

The decision of the Court below cannot be reconciled with the position of the Seventh Circuit in *Blank* v. *Bitker*, 135 F. 2d 962 (CCA 7, 1943), of the Third Circuit in *Orange Theatre Corp.* v. *Rayherstz Amusement Corp.*, 139 F. 2d 871

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[1] Recently, in *Proctor* v. *The Sagamore Big Game Club*, D. C. W. D. Pa., 128 F. Supp. 885 (1955), the Court took cognizance of the conflict of jurisdictional opinion which now exists but it concluded that "the best view on this subject is the decision in *McQuillen* v. *National Cash Register Co.*, 4 Cir., 112 F. 2d 887 • • •".

(CCA 3, 1944), cert. den. 322 U. S. 740, and of the Eighth Circuit in *Vilter Mfg. Co.* v. *Rolaff*, 110 F. 2d 491 (CCA 8, 1940).

Rule 12(b), Federal Rules of Civil Procedure, provides that no defense is waived by being joined with one or more defenses in a responsive pleading. The decision below referred to this rule but found that its purpose was only to eliminate the hoary ritual of special appearances and that it did not compel a result contrary to the position it had taken.

However, the Court below refused to recognize that the rule was intended to afford a safeguard for a defendant who would contest a Court's jurisdiction. The Court of Appeals for the Third Circuit in *Orange Theatre Corp.* v. *Rayherstz Amusement Corp.*, *supra*, aptly described the purpose of Rule 12 (b) as follows:

> "A defendant need no longer appear specially to attach the court's jurisdiction over him. He is no longer required at the door of the federal courthouse to intone that ancient abracadabra of the law, *de bene esse*, in order by its magic power to enable himself to remain outside even while he steps within. He may now enter openly in full confidence that he will not thereby be giving up any keys to the courthouse door which he possessed before he came in. * * *"

Can a defendant risk stepping into the courthouse knowing that if his challenge to the jurisdiction should fail, he will find the courthouse exits blocked?

Such is the interpretation of the Court below. In this it is squarely opposed to the views of the Courts of Appeal for the Third Circuit, the Fourth Circuit, the Sixth Circuit, the Seventh Circuit, the Eighth Circuit and the Ninth Circuit.

The Court below stated that "it also seems probable that under F. R. 4(d)(1) personal jurisdiction over Balanovski

and probably also over Horenstein was acquired by service of process on their agent Miss Devine." Authorization to receive such process was spelled out by the Court from a limited and special power of attorney (Pets.' App. 52-6) given by Balanovski to Miss Devine before his departure from the United States[1]. The conclusion in the decision below that such a power of attorney could constitute "an implied actual appointment" to receive process within the meaning of F. R. 4(d)(1) is completely unsound and directly in conflict with the principles expressed in *Osterling* v. *Commonwealth Trust*, 35 F. Supp. 704 (D. C. W. D. Pa., 1940), *aff'd* 115 F. 2d 809 (CCA 3, 1940).

Rule 4(d)(1) provides briefly that "Service shall be made * * * by delivering a copy of the summons and of the complaint to an agent authorized by appointment or by law to receive service of process". It is clear that the powers set forth in the special power of attorney here involved[2] do not cloak the appointee with the specific authority to receive service of process required under the statute.

The Court of Appeals for the Third Circuit in *Osterling* v. *Commonwealth Trust, supra,* in a *per curiam* decision based upon the opinion below, upheld the District Court's determination that a power of attorney specifically authorizing a co-executor to accept service in any action arising out of the administration of an estate, was insufficient to empower the agent to accept service in an action against the executor as a tort feasor in his personal capacity.

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[1] It should be observed that the respondent herein never contended that the power of attorney could be deemed an authorization to accept service on behalf of Horenstein. In fact the District Court found only that this document was sufficient to give the Court *in personam* jurisdiction over Balanovski (Pets.' App. 25-6).

[2] The power of attorney authorized Miss Devine to engage in a number of specified transactions with certain trust companies and then, in a general clause, gave her power to perform every act necessary "in the premises" (Pets.' App. 52-6).

It was the view of the Court that the authority to accept service must be plainly specified and that the courts should not extend such authority beyond its precise limits. This interpretation is obviously inconsistent with the view of the Court below in the present case.

Here the District Court's *in rem* jurisdiction, if such existed,[1] could not exceed the sum of $554,185.07 on deposit with two New York banks. However, a determination that personal jurisdiction had been obtained permitted the entry of personal judgments against the petitioners aggregating eight million dollars.

II.

Important questions of Federal tax law are presented which should be settled by this Court.

A. Source of Income.

This case involves fundamental questions of widespread importance in the law of taxation of non-resident aliens. The same principles are also controlling in the taxation of Western Hemisphere Trade Corporations.

Non-resident aliens engaged in a trade or business in the United States are subject to tax only upon income from sources within the United States.[2] Income earned by non-resident aliens from the purchase of personal property

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[1] Petitioners question whether the District Court in fact had *in rem* jurisdiction, since the bank deposits levied upon belonged to Cadic and not to the individual partners (Pets.' App. 21-4). *United States* v. *Worley*, 213 F. 2d 509 (CCA 6, 1954), cert. denied, 348 U. S. 917, 918 (1955).

[2] Section 212(a), Internal Revenue Code of 1939. If the alien is not engaged in business in the United States, he is taxable only upon certain types of income which are "fixed or determinable annual or periodic gains, profits and income . . ." within the meaning of Section 211(a)(1)(A).

within and its sale without the United States is treated as derived entirely "from sources within the country in which sold. . . ."[1]

The fundamental question presented is what factors are decisive in determining the place of sale for the purpose of ascertaining the source of income. The place of sale is not defined by the statute and the Commissioner's regulations specify only that it "ordinarily means the place where the property is marketed".[2]

The identical questions of the source of income and the place of sale are of vital concern to taxpayers seeking to qualify as Western Hemisphere Trade Corporation.[3] The Regulations applicable to Section 109[4] specify that these questions "shall be determined as provided in Section 119 and the Regulations prescribed thereunder". The final decision in this case, therefore, will directly affect many taxpayers claiming benefits granted Western Hemisphere Trade Corporations. Some of these are already involved in litigation on the identical questions and these will be fully resolved by a review of the decision below.

* * * * * *

In 1930 a Treasury ruling was published (G. C. M. 8594, IX-2 Cum. Bull. 354, *infra*, Appendix D) for the purpose of clarifying the Commissioner's interpretation

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[1] Section 119(e), Internal Revenue Code of 1939.

[2] Regulation 111, Sec. 29.119-8.

[3] Section 109 defines a Western Hemisphere Trade Corporation as being a domestic corporation all of whose business is done in any country or countries in North, Central or South America, or in the West Indies, or in Newfoundland, and which (a) derives 95% or more of its gross income (for the three-year period immediately preceding the close of the taxable year) from sources without the United States; and (b) which derives 90% or more of the gross income from the active conduct of a trade or business.

[4] Regulation 111, Sec. 29.109-1.

of the statutory phrases in question. The ruling was founded upon a decision of this Court rendered shortly prior thereto in *Compania General de Tabacos de Filipinas* v. *Collector*, 279 U. S. 306 (1929). Referring to this decision the ruling stated (Appendix D, *infra*, pp. 27a-28a):

> "The decision is conclusive that the technical rules as to the passing of the property in the goods and the assumption of risk are not determinative of the place of sale and the source of income from the sale of goods. The essential character of the transaction—the contract of sale—is the decisive factor in determining the place of sale for the purpose of determining the source of income." * * *
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> "*Compania General de Tabacos de Filipinas* v. *Collector* is therefore conclusive that, for the purpose of determining the place of sale so far as this is decisive of the source of income, 'the substance of the sale is the agreement to sell'. (*Norfolk & Western Railway Co. Sims*, 191 U. S. 411, 447)."

This was the official Treasury interpretation for a period of 17 years.[1] Aliens and citizen taxpayers alike ordered their business affairs in accordance with and in reliance on this official interpretation which had been long and consistently followed by the Treasury.

In November of 1947 (after the sales transactions here involved had been completed and Balanovski had departed these shores), the aforesaid ruling was revoked by G. C. M. 25131 (1947-2 Cum. Bull. 85, *infra*, Appendix E). In this

[1] The Treasury adhered to this interpretation notwithstanding the conflicting position taken by the Board of Tax Appeals in East Coast Oil Co., S. A., 31 B. T. A. 558 (1934), aff'd, 85 F. 2d 322 (5 Cir. 1936), cert. den., 299 U. S. 608; Elston Co., Ltd., 42 B. T. A. 208 (1940); Ronrico Corp., 44 B. T. A. 1130 (1941); Exolon Co., 45 B. T. A. 844 (1941).

ruling the Treasury reversed the position above stated and held that the technical rule—the place where title to the property passes to the buyer—is decisive in determining the place of sale within the meaning of Section 119(e).

While the 1947 ruling adopts the aforesaid "passage-of-title" test as a "general rule", it applies a more realistic test in those cases where the transaction has been arranged so as to avoid the tax. The ruling provides (Appendix E, *infra*, p. 31a):

> "In such cases, all factors of the transaction, such as negotiations, the execution of the agreement, the location of the property, and the place of payment, will be considered, and the sale will be treated as having been consummated at the place where the substance of the sale occurred."

The District Court below refused to concur in a rule in which the incidence of tax in two substantially identical transactions would depend solely upon the "witty diversities" of the law which determined when and where title passed to the buyer. It decided, rather, that in every case all of the factors of the transaction should be considered in determining where the property had been sold.

The Court of Appeals disagreed with the interpretation. It conceded that the present Treasury rule stated in G. C. M. 25131 had obvious infirmities and produced inequitable results, but it nevertheless adhered to it for lack of a "suitable substitute test providing an adequate degree of certainty for taxpayers".

This construction by the Court below, however, has not created certainty among taxpayers. On the contrary, only uncertainty now exists since taxpayers have no assurance as to when the Treasury will apply the "passage of title" test and when, charging tax avoidance, it will apply the "substance of the sale" rule.

As a consequence of this interpretation of the statute, foreign purchasers of American merchandise destined for resale in their own countries are in jeopardy of incurring United States income taxes if they finance their purchases by the usual form of letter of credit.[1] As the District Court noted in its decision below, this can "only deter foreign business organizations from purchasing goods in the United States and from engaging the services of banking institutions located in the United States. It seems clear that Congress did not intend such a result" (Pets.' App. 13).

Another anomalous result is that a non-resident alien may actively conduct a business within the United States, enter into contracts of sale with American citizens here, and, by arranging for the transfer of title at a foreign port, escape any tax upon the income from such sales. Only if the Treasury can establish a tax avoidance motive, so as to make applicable the "substance of the sale" test, would taxes be levied here on income from sales made within the United States. This interpretation does not implement the Congressional intention to tax all income from sources within the United States.

These questions have received brief consideration from this Court in *Compania General de Tabacos de Filipinas* v. *Collector of Internal Revenue,* 279 U. S. 306 (1929), but the Court was not there construing the Internal Revenue Code or precisely the same statutory language.[2] Moreover, the

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[1] It is common knowledge that substantially all export business to Central and South America is done under assignable letters of credit under arrangements whereby the beneficial title passes at an American port.

See Finkelstein: Legal Aspects of Commercial Letters of Credit (1930); Thayer, C. I. F. Contracts in International Commerce, 53 Harv. L. Rev. 792 (1940).

[2] A Philippine income tax statute was there involved which imposed a tax on income "from all sources within the Philippine Islands . . .".

application of that decision to the statute now under consideration is far from clear. Advocates of conflicting interpretations of this statute have each cited and relied upon this decision as supporting their respective views.[1]

In *Compania General* it was held that if the confirmation of the contract was given in the Philippines (where the taxpayer maintained a branch office) and the contract was thus completed, "the final acts of the petitioner making effective the sales, which were the cause of the profit, took place in the Philippine Islands as an incident to and part of its business conducted there." Furthermore, this Court determined that if the sale was thus made in the Philippines it was "unimportant whether the merchandise sold was exported before or after its sale * * *".

The vital question with which the Court was concerned was whether the contract was completed in the United States or in the Philippine Islands. Passage of title to the goods, which would occur when the merchandise was exported, was deemed to be totally unimportant.

Yet, the decision in *Compania General* has in some inexplicable fashion been advanced as authority for the proposition that the passage of title is the final act completing a sale and, therefore, is the sole controlling factor in the determination of "the country in which sold".[2] The Court below fell into the same error.

A clarification of the rule expressed in *Compania General* is vital to dispel the confusion and uncertainty now existing in this area of the tax law. The Court below

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[1] In G. C. M. 8594 (IX-2 Cum. Bull. 354) the Treasury's "substance of the sale" rule was enunciated because of the Court's language in the *Compania General*. The Board of Tax Appeals in *East Coast Oil Co., S. A.*, 31 B. T. A. 558 (1934) cited *Compania General* as supporting its "passage of title" test.

[2] Section 119(e).

admitted that it advocated the "passage of title" test for lack of a better rule and that the rule might be subject to criticism as being inequitable. Not only is it inequitable but it is also unsound and should be reviewed by this Court.

B. Doing Business in the United States.

Can an Argentine citizen whose only function in the United States was to purchase merchandise for resale to a single Argentine customer be deemed to be engaged in a trade or business within the United States?

The Court below reversed the District Court and held that these activities (coupled with its finding that Cadic's sales were completed here) constituted the conduct of a trade or business in the United States. The District Court's summary of the facts was as follows (Pets.' App. 13):

> "Balanovski's activities in the United States were those of a purchasing agent. He located suppliers, inspected the goods that they had to sell, and took care of the details of paying the suppliers and of shipping the goods to Argentina."

However, the Court below supplemented these facts with a determination that Balanovski was engaged in selling merchandise within the United States because it had decided that Cadic's sales to IAPI, by reason of the passage of title, were actually consummated here. In other words, the Court concluded that a non-resident purchasing and exporting goods, directly or by an agent, will be deemed to be engaged in business in this country if as an incidence of resale the title to the goods passes to the ultimate purchaser in the United States.

This is a novel doctrine without precedent in the law.

It has long been the position of the Treasury Department that the purchase of goods in the United States for

resale outside the country was not the conduct of a trade or business. 32 Op. A. G. 336 (1920).

Treasury Decision 3111, C. B., June 1921, page 280, referring to the aforesaid opinion of the Attorney General, states in part:

> "The mere buying of goods within the United States, with capital from abroad, to be sold abroad, is not a trade or business exercised in the United States so as to subject the purchaser of the goods to income taxes. A merchant exercises his trade where he has his principal place of business, viz., where his profits come home to him."

In *Deputy* v. *Dupont*, 308 U. S. 488 (1940) this Court defined the conduct of a trade or business, stating at page 499:

> "Carrying on any trade or business within the contemplation of Section 23(a) involves holding oneself out to others as engaged in the selling of goods or services."

Cadic had no customers in the United States. Neither Cadic nor its representative, Balanovski, held itself out as prepared to sell goods to anyone in the United States. It was merely buying supplies here, and the technical rules governing the passage of title cannot serve to convert such buying activities into the conduct of a trade or business within the United States.

The determination that aliens buying goods in the United States, implemented by letters of credit as here, are deemed to be doing business in this country will have a far reaching effect. It is unavoidable that such a decision will be a deterrent to foreign purchasing activities in this country and will place an unnecessary burden upon our

export trade. This can hardly be consistent with Congressional intention.

C. Retroactive Revocation of C. C. M. 8594.

In 1947, when the sales transactions in the present case were consummated, the Commissioner's ruling in G. C. M. 8594 was the official interpretation of Section 119(e). This widely publicized ruling and the applicable regulations were in effect for a period of 17 years, during which period the statute was reenacted by Congress without substantial change.

Petitioners in the present case conducted their sales so that, in accordance with and reliance upon the published ruling, it would not be contended that income therefrom arose from sources within the United States. In November of 1947, after these sales had been completed and Balanovski had returned to Argentina, the Treasury reversed its ruling with retroactive effect.

The question of whether the Commissioner of Internal Revenue may retroactively revoke a published ruling which has been long and consistently followed is a matter of vital importance to all taxpayers. Taxpayers' rulings and published rulings have been issued by the Treasury in increasing numbers in recent years.[1] Their place in the administration of our tax laws is well established. But the usefulness of this practice to taxpayers and the Treasury depends largely upon whether such rulings may with impunity be relied upon by all taxpayers. If they cannot be relied upon, and if they may be revoked retroactively whenever the Commissioner finds it convenient or desirable to do so, such rulings serve only as traps for the unwary.

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[1] See, Annual Report of the Commissioner of Internal Revenue for the Fiscal Year ended June 30, 1955 (House Document No. 246, 84th Cong. 2d Sess.).

Section 3791(b) of the Code[1] does not authorize the Commissioner to make a retroactive ruling. This Court has held in *Helvering* v. *R. J. Reynolds Tobacco Co.*, 306 US 110 (1939), that Section 3791(b) is inapplicable where the Commissioner does not have the power to make a retroactive ruling, as in cases where Congress by repeatedly reenacting a statute has impliedly given its sanction to an existing ruling or regulation.

This question, as it applies to taxpayers' rulings, was passed upon in *Automobile Club of Michigan* v. *Commissioner*, 230 F. 2d 585 (CCA 6, 1956). A petition for certiorari filed by the taxpayer therein on May 15, 1956 raises this issue as one of the questions presented for review. This Court granted certiorari on October 8, 1956.

If this Court should decide upon hearing that appeal that the Commissioner of Internal Revenue may not retroactively revoke published rulings to the detriment of taxpayers who have relied upon them, the petitioners in the present case would be entitled to a reversal of the judgment below. However, unless certiorari is also granted in the present case the rights of the petitioners will not be preserved until the Court has made its determination.

Conclusion.

This petition for a writ of certiorari should be granted.

Respectfully submitted,

DONALD L. STUMPF,
SANDOW HOLMAN,
Counsel for Petitioners.

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[1] Appendix A, *infra*, p. 2a.

Appendix A.

Statutes, Regulations and Rules Involved

Rules of Civil Procedure, 28 U. S. C.:

4. Process

(d) Summons: * * * Service shall be made as follows:

(1) Upon an individual * * * by delivering a copy of the summons and of the complaint to him personally or * * * to an agent authorized by appointment or by law to receive service of process.

12. Defenses and Objections—* * *

(b) How Presented. Every defense, in law or fact, to a claim for relief in any pleading, * * * shall be asserted in the responsive pleading thereto if one is required, * * *. No defense or objection is waived by being joined with one or more other defenses or objections in a responsive pleading or motion. * * *

Internal Revenue Code of 1939:

Sec. 119. Income from Sources within United States.

(e) Income from Sources Partly within and Partly without United States.

* * * * * *

* * * Gains, profits and income derived from the purchase of personal property within and its sale without the United States or from the purchase of personal property without and its sale within the United States, shall be treated as derived entirely

from sources within the country in which sold, except that gains, profits and income derived from the purchase of personal property within a possession of the United States and its sale within the United States shall be treated as derived partly from sources within and partly from sources without the United States.

Sec. 212. Gross Income.

(a) General Rule.—In the case of a nonresident alien individual gross income includes only the gross income from sources within the United States.

Sec. 3791. Rules and Regulations.

* * * * * *

(b) Retroactivity of Regulations or Rulings.—The Secretary, or the Commissioner with the approval of the Secretary, may prescribe the extent, if any, to which any ruling, regulation, or Treasury Decision, relating to the internal revenue laws, shall be applied without retroactive effect.

Treasury Regulations 111:

Sec. 29.119-8. Sale of personal property.—

Income derived from the purchase and sale of personal property shall be treated as derived entirely from the country in which sold, * * *

* * * * * *

The "country in which sold" ordinarily means the place where the property is marketed.

Sec. 29.212-1.

(a) No United States business.—

The gross income of a nonresident alien individual not engaged in trade or business within the United States at any time during the taxable year, whether such alien comes within section 211(a) or section 211(c), is gross income from sources within the United States, consisting of fixed or determinable annual or periodical income * * *

Appendix B.

Opinion.

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT.

No. 369—October Term, 1955.

(Argued June 4, 1956 Decided August 14, 1956.)

Docket No. 23853

UNITED STATES OF AMERICA,

Plaintiff-Appellee,

v.

ISRAEL BALANOVSKI, SAMUEL BERNARDO HORENSTEIN, COMPANIA ARGENTINA DE INTERCAMBIO COMERCIAL, I. BALANOVSKI & CIA. (sometimes called "CADIC"), a co-partnership,

Defendants-Appellants.

Before:

CLARK, *Chief Judge*, and HINCKS and WATERMAN, *Circuit Judges*.

Appeal from the United States District Court for the Southern District of New York, Edmund L. Palmieri, *Judge*.

Both the defendant taxpayers and the United States of America appeal from a decision, D. C. S. D. N. Y., 131 F. Supp. 898, granting a judgment against the defendants for income taxes for 1947 on profits on sales of personal property shipped to Argentina. Reversed and remanded on the appeal of the United States of America.

MAURICE N. NESSEN, Asst. U. S. Atty., S. D. N. Y., New York City (Paul W. Williams, U. S. Atty., and Arthur B. Kramer, Asst. U. S. Atty., New York City, on the brief), *for plaintiff-appellee.*

DONALD L. STUMPF, New York City (Sandow Holman, New York City, on the brief), *for defendants-appellants.*

CLARK, Chief Judge:

This is an appeal by defendants and a cross-appeal by the United States of America from a decision of Judge Palmieri, sitting without a jury, adjudging defendant-taxpayers liable for almost $1,000,000 in income taxes and interest for the year 1947, and directing two New York banks to pay over funds belonging to the defendant partnership in part payment of the judgment. D. C. S. D. N. Y., 131 F. Supp. 898. In our view the recovery granted was insufficient, and we are therefore reversing on the appeal of the United States only.

Defendants Balanovski and Horenstein were copartners in the Argentine partnership, Compania Argentina de Intercambio Comercial (CADIC), Balanovski having an 80 per cent interest and Horenstein, a 20 per cent interest. Balanovski, an Argentinian citizen, came to the United States on or about December 20, 1946, and remained in this country for approximately ten months, except for an absence of a few weeks in the spring of 1947 when he returned to Argentina. His purpose in coming here was the transaction of partnership business; and while here, he made extensive purchases and sales of trucks and other equipment resulting in a profit to the partnership of some $7,763,702.20.

His usual mode of operation in the United States was to contact American suppliers and obtain offers for the sale of equipment. He then communicated the offers to his father-in-law, Horenstein, in Argentina. Horenstein, in turn, submitted them at a markup to an agency of the

Argentine Government, Instituto Argentino de Promocion del Intercambio (IAPI), which was interested in purchasing such equipment. If IAPI accepted an offer, Horenstein would notify Balanovski and the latter would accept the corresponding original offer of the American supplier. In the meantime IAPI would cause a letter of credit in favor of Balanovski to be opened with a New York bank. Acting under the terms of the letter of credit Balanovski would assign a portion of it, equal to CADIC's purchase price, to the United States supplier. The supplier could then draw on the New York bank against the letter of credit by sight draft for 100 per cent invoice value accompanied by (1) a commercial invoice billing Balanovski, (2) an inspection certificate, (3) a nonnegotiable warehouse or dock receipt issued in the name of the New York bank for the account of IAPI's Argentine agent, and (4) an insurance policy covering all risks to the merchandise up to delivery F.O.B. New York City. Then, if the purchase was one on which CADIC was to receive a so-called quantity discount or commission, the supplier would pay Balanovski the amount of the discount. These discounts, paid after delivery of the goods and full payment to the suppliers, amounted to $858,595.90, constituting funds which were delivered in the United States.

After the supplier had received payment, Balanovski would draw on the New York bank for the unassigned portion of the letter of credit, less 1 per cent of the face amount, by submitting a sight draft accompanied by (1) a commercial invoice billing IAPI, (2) an underaking to ship before a certain date, and (3) an insurance policy covering all risks to the merchandise up to delivery F.A.S. United States Sea Port. The bank would then deliver the nonnegotiable warehouse receipt that it had received from the supplier to Balanovski on trust receipt and his undertaking to deliver a full set of shipping documents, including a clean on board bill of lading issued to the order of IAPI's Argentine agent, with instructions to notify IAPI. It would also notify the warehouse that Balanovski was authorized to withdraw the merchandise. Upon delivery of these shipping

documents to the New York bank Balanovski would receive the remaining 1 per cent due under the terms of the letter of credit. Although Balanovski arranged for shipping the goods to Argentina, IAPI paid shipping expenses and made its own arrangement there for marine insurance. The New York bank would forward the bill of lading, Balanovski's invoice billing IAPI, and the other documents required by the letter of credit (not including the supplier's invoice billing Balanovski) to IAPI's agent in Argentina.

Twenty-four transactions following substantially this pattern took place during 1947. Other transactions were also effected which conformed to a substantially similar pattern, except that CADIC engaged the services of others to facilitate the acquisition of goods and their shipment to Argentina. And other offers were sent to Argentina, for which no letters of credit were opened. Several letters of credit were opened which remained either in whole or in part unused. In every instance of a completed transaction Balanovski was paid American money in New York, and in every instance he deposited it in his own name with New York banks. Balanovski never ordered material from a supplier for which he did not have an order and letter of credit from IAPI.

Balanovski's activities on behalf of CADIC in the United States were numerous and varied and required the exercise of initiative, judgment, and executive responsibility. They far transcended the routine or merely clerical. Thus he conferred and bargained with American bankers. He inspected goods and made trips out of New York State in order to buy and inspect the equipment in which he was trading. He made sure the goods were placed in warehouses and aboard ship. He tried to insure that CADIC would not repeat the errors in supplying inferior equipment that had been made by some of its competitors. And while here he attempted "to develop" "other business" for CADIC.

Throughout his stay in the United States Balonovski employed a Miss Alice Devine as a secretary. She used,

and he used, the Hotel New Weston in New York City as an office. His address on the documents involved in the transactions was given as the Hotel New Weston. His supplier contacted him there, and that was the place where his letters were typed and his business appointments arranged and kept. Later Miss Devine opened an office on Rector Street in New York City, which he also used. When he returned to Argentina for a brief time in 1947 he left a power of attorney with Miss Devine. This gave her wide latitude in arranging for shipment of goods and in signing his name to all sorts of documents, including checks. When he left for Argentina again at the end of his 10-month stay, he left with Miss Devine the same power of attorney,[1] which she used throughout the balance of 1947 to arrange for and complete the shipment of goods and bank the profits.

When Balanovski left the United States in October 1947 he filed a departing alien income tax return, on which he reported no income. In March 1948 the Commissioner of Internal Revenue assessed $2,122,393.91 as taxes due on income for the period during which Balanovski was in the United States. In May 1953 the Commissioner made a jeopardy assessment against Balanovski in the amount of $3,954,422.41 and gave him notice of it. At the same time a similar jeopardy assessment, followed by a timely notice of deficiency, was made against Horenstein in the amount of $1,672,209.90, representing his alleged share of CADIC's profits on the above-described sales of United States goods.

The government brought the present action to foreclose a federal tax lien on $511,655.58 and $42,529.49—amounts

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[1] The power of attorney consisted of 13 paragraphs covering such topics as "Endorsement for Deposit," "Signing checks and settling accounts," "Acceptances," "Procuring Discounts," "Sale of securities," "Borrowing and giving security," "Letters of Credit," and "Contracts."

One of these paragraphs read as follows:

"(General authority and substitution)—Give unto said attorney(s) full power and authority to do and to perform every act whatsoever requisite and convenient to be done in the premises as fully as I might do if personally present with full power of substitution and revocation hereby ratifying all that my said attorney(s) or the substitute(s) shall do or cause to be done by virtue hereof;"

of partnership funds held in two United States banks—and to obtain personal judgments against Balanovski and Horenstein in the sums of $6,722,625.54 (of which $5,050,415.64 is now sought on appeal) and $1,672,209.90 respectively. Balanovski and Horenstein were served with process by mail in Argentina pursuant to 28 U. S. C. §1655; and Miss Devine, the purported agent of Balanovski, was personally served in New York. Defendants then appeared by their attorneys and proceeded to defend the action.

JURISDICTION OF THE DISTRICT COURT.

Defendants challenge the court's jurisdiction (1) *quasi-in-rem,* because the assets levied upon were the property of the partnership, rather than of the individual taxpayers, and (2) *in personam,* because the defendants were not personally served with process and they contend that Miss Devine was not Balanovski's agent "authorized by appointment or by law to receive service of process" under F. R C. P., rule 4(d)(1).

Quasi-in-rem jurisdiction in this case is based on enforcement of a tax lien under §§3670 and 3678(a) of the Internal Revenue Code of 1939. These sections permit an action *quasi-in-rem* against named defendants to recover any "property owned by the delinquent, or in which he has any right, title, or interest." This grant of jurisdiction is sufficient to reach a partner's interest in partnership property. See *Kamen Soap Products Co.* v. *C. I. R.,* 2 Cir., 230 F. 2d 565; N. Y. Partnership Law §§50-52; *United States* v. *Dallas Nat. Bank,* 5 Cir., 152 F. 2d 582; *United States* v. *Dickerson,* D. C. E. D. Mo., 101 F. Supp. 262. Cf. *United States* v. *Kensington Shipyard & Drydock Corp.,* 3 Cir., 169 F. 2d 9, 12. Whether the government can gain execution on any portion of the partnership assets is not a question of jurisdiction, but one of execution and of priority among the government, partnership creditors, and other partners. In any event, the assets here reached are partnership *profits* which are presumably not burdened by the claims of creditors.

Since the defendants appeared and defended on the merits, the court acquired power to render a judgment *in personam* conditional only upon the validity of the original *quasi-in-rem* jurisdiction. The parties cannot complain of inconvenience, since they have come into the jurisdiction. They have had their day in court on the issues which would settle both the right to the funds and personal liability; there is no constitutional problem. See Blume, *Actions Quasi in Rem under Section 1655, Title 28, U. S. C.*, 50 Mich. L. Rev. 1, 22. If the parties or if other assets are found in the United States, a rule against personal jurisdiction will only bring on further litigation, which the taxpayers will lose on the merits by collateral estoppel or *stare decisis*. Thus a rule against personal jurisdiction would be merely a mandate for further fruitless litigation. While this point has provoked some conflict, we regard the cases so agreeing as stating the better rule. *Anderson* v. *Benson*, D. C. Neb., 117 F. Supp. 765; *Grant* v. *Kellogg Co.*, D. C. S. D. N. Y., 3 F. R. D. 229; *Bede Steam Shipping Co.* v. *New York Trust Co.*, D. C. S. D. N. Y., 54 F. 2d 658; *Campbell* v. *Murdock*, D. C. N. D. Ohio, 90 F. Supp. 297; 2 Moore's Federal Practice ¶12.13 (2d Ed. 1948). For the contrary view see *Salmon Falls Mfg. Co.* v. *Midland Tile & Rubber Co.*, 6 Cir., 285 F. 214; *McQuillen* v. *National Cash Register Co.*, 4 Cir., 112 F. 2d 877, certiorari denied 311 U. S. 695, rehearing denied 311 U. S. 729; *Proctor* v. *The Sagamore Big Game Club*, D. C. W. D. Pa., 128 F. Supp. 885; cf. *Fahey* v. *O'Melveny & Myers*, 9 Cir., 200 F. 2d 420. F. R. 12(b), permitting the filing of objections to jurisdiction and on the merits at the same time, does not compel a contrary result; the purpose of that rule is to permit a party to challenge jurisdiction along with his other defenses and without going through the hoary ritual of entering a special appearance. There is no indication that the rule was intended to be so tortuously construed in circumstances like the present to promote unnecessary litigation.

It also seems probable that under F. R. 4(d)(1) personal jurisdiction over Balanovski and probably also over Horen-

stein was acquired by service of process on their agent Miss Devine. The power of attorney granted to Miss Devine by Balanovski at his departure was broad and sweeping in its terms, and an implied actual appointment to receive service of process may be readily spelled out therefrom. Cf. *Cohen* v. *Physical Culture Shoe Co., Division of Orthopedic Shoes,* D. C. S. D. N. Y., 28 F. Supp. 679, 680; *Fleming* v. *Malouf,* D. C. W. D. N. Y., 7 F. R. D. 56; *Szabo* v. *Keeshin Motor Exp. Co.,* D. C. N. D. Ohio, 10 F. R. D. 275; *Morfessis* v. *Marvins Credit, Inc.,* D. C. Mun. Ct. App., 77 A. 2d 178; *Osterling* v. *Commonwealth Trust Co. of Pittsburgh,* D. C. W. D. Pa., 35 F. Supp. 704, affirmed 3 Cir., 115 F. 2d 809, 1940. In fact Miss Devine filed a federal income tax return for Balanovski after his departure in which she described herself as his "agent." Since the applicable Regulations[2] apparently render her responsible for the filing of Balanovski's tax returns and the payment of his tax out of the funds which flowed through her hands and since she actually filed a return for Balanovski, she may be responsible for any taxes found owing on that return. All these circumstances, it seems, may result in her authorization by operation of law (in addition to her appointment in fact) to receive service of process for Balanovski in this action to collect taxes owed by him. The district court therefore has jurisdiction of this action.

The Merits

The district court held that CADIC was not engaged in a trade or business within the United States within the meaning of §219 of the Internal Revenue Code of 1939, but that each of the partners was liable for certain taxes because Balanovski as an individual was so engaged in business and therefore taxable under §211(b), while Horenstein received "fixed or determinable annual or periodical gains, profits, and income" within the meaning of §211(a)(1)(A) and (c). We, on the contrary, hold that the partnership CADIC *was* engaged in business in the United States and that hence the two copartners were taxable for

[2] See Treas. Reg. 118, §§39.217-2(b)(2), 39.51-2.

their share of its profits from sources within the United States. The applicable statutes are §§211(b), 212, and 219 of the Internal Revenue Code of 1939.

CADIC was actively and extensively engaged in business in the United States in 1947. Its 80 per cent partner, Balanovski, under whose hat 80 per cent of the business may be thought to reside, was in this country soliciting orders, inspecting merchandise, making purchases, and (as will later appear) completing sales. While maintaining regular contact with his home office, he was obviously making important business decisions. He maintained a bank account here for partnership funds. He operated from a New York office through which a major portion of CADIC's business was transacted. See *C. I. R.* v. *Nubar*, 4 Cir., 185 F. 2d 584, 588, certiorari denied 341 U. S. 925; *Fernand C. A. Adda*, 10 T. C. 273, 277, 278, affirmed per curiam *Adda* v. *C. I. R.*, 4 Cir., 171 F. 2d 457, certiorari denied 336 U. S. 952; *Pinchot* v. *C. I. R.*, 2 Cir., 113 F. 2d 718, 719; *Jan Casimir Lewenkaupt*, 20 T. C. 151, 163.

We cannot accept the view of the trial judge that, since Balanovski was a mere purchasing agent, his presence in this country was insufficient to justify a finding that CADIC was doing business in the United States. We need not consider the question whether, if Balanovski (an 80 per cent partner) were merely engaged in purchasing goods here, the partnership could be deemed to be engaged in business, since he was doing more than purchasing. Acting for CADIC he engaged in numerous transactions wherein he both purchased and sold goods in this country, earned his profits here, and participated in other activities pertaining to the transaction of business. Cases cited in support of the proposition that CADIC was not engaged in business here are quite distinguishable. Cf. *The Linen Thread Co., Ltd.*, 14 T. C. 725; *Jorge Pasquel*, 12 T. C. M. 1431; *The Amalgamated Dental Co., Ltd.*, 6 T. C. 1009; *European Naval Stores Co., S. A.*, 11 T. C. 127; *R. J. Dorn & Co.*, 12 B. T. A. 1102.

As copartners of CADIC, Balanovski and Horenstein are taxable for the amount of partnership profits from

sources within the United States under the statutory provisions cited above. The district court held them taxable only upon the "discounts" or "commissions" paid CADIC by the suppliers after completion of the sales transactions, not upon the total profits of the sales. This solution of the problem is in seeming conflict with the usual rule that discounts received as inducements for quality purchasing are considered as reducing the purchasers' cost for tax purposes. See *C. I. R.* v. *Bullock's*, 9 Cir., 81 F. 2d 1002. Further, isolation of the discount from the sales transaction is not in accord with preferred accounting technique. See, *e.g.*, Paton, Essentials of Accounting 264-266 (Rev. Ed. 1949). But see Finney, General Accounting 247-250 (1946). Isolation of the discount for tax purposes would be more appropriate if the court considered the partnership as a broker receiving commissions, rather than as a vendor. Cf. *Simon* v. *C. I. R.*, 2 Cir., 176 F. 2d 230. See Note, 69 Harv. L. Rev. 567, 568-569. But we need not consider whether the circumstances here justified the segregation for tax purposes of the discounts from the remainder of the sales profits—see *G. A. Stafford & Co.* v. *Pedrick*, D. C. S. D. N. Y., 78 F. Supp. 89, affirmed 2 Cir., 171 F. 2d 42—for we hold the total profits on these transactions, including the discounts, to be taxable in full.

Under §119(a)(6) and (e)[3] of the 1939 Code, a nonresident alien engaged in business here derives income

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[3] Internal Revenue Code of 1939:

"§119. *Income from sources within United States*

"(a) *Gross income from sources in United States.* The following items of gross income shall be treated as income from sources within the United States:

* * * * *

"(6) *Sale of Personal Property.* For gains, profits, and income from the sale of personal property, see subsection (e).

* * * * *

"(e) *Income from sources partly within and partly without United States.* Items of gross income, expenses, losses and deductions, other than those specified in subsections (a) and (c) of this section, shall be allocated or apportioned to sources within or without the United States, under rules and regulations prescribed by the Commissioner with the approval of the Secretary. * * * Gains, profits and income derived from the purchase of personal property with-

from the sale of personal property in "the country in which [the goods are] sold." By the overwhelming weight of authority, goods are deemed "sold" within the statutory meaning when the seller performs the last act demanded of him to transfer ownership, and title passes to the buyer. See *East Coast Oil Co., S. A.*, 31 B. T. A. 558, affirmed *C. I. R.* v. *East Coast Oil Co., S. A.*, 5 Cir., 85 F. 2d 322, certiorari denied *Helvering* v. *East Coast Oil Co., S. A.*, 299 U. S. 608; *Amtorg Trading Corp.* v. *Higgins*, 2 Cir., 150 F. 2d 536, 539; *G. A. Stafford & Co.* v. *Pedrick, supra*, D. C. S. D. N. Y., 78 F. Supp. 89, affirmed without reaching the point, 2 Cir., 171 F. 2d 42; *Ronrico Corp.*, 44 B. T. A. 1130, 1136; *The Exolon Co.*, 45 B. T. A. 844; *Askania Werke, A. G.*, 33 B. T. A. 875, remanded for evidence, *Askania Werke, A. G.* v. *Helvering*, D. C. Cir., 96 F. 2d 717; *Elston Co., Ltd.*, 42 B. T. A. 208; *Hazelton Corp.*, 36 B. T. A. 908; *Tootal Broadhurst Lee Co., Ltd.*, 9 B. T. A. 321; *Compania General de Tabacos de Filipinas* v. *Collector of Internal Revenue*, 279 U. S. 306, 309; *American Land & Investment Co.* v. *C. I. R.*, 4 Cir., 40 F. 2d 336; *Ardbern Co.*, 41 B. T. A. 910, affirmed on the point, *Ardbern Co.* v. *C. I. R.*, 4 Cir., 120 F. 2d 424; *Briskey Co.*, 29 B. T. A. 987, affirmed *C. I. R.* v. *Briskey Co.*, 3 Cir., 78 F. 2d 816; *Sabatini* v. *C. I. R.*, 2 Cir., 98 F. 2d 753, 755.[4]

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in and its sale without the United States or from the purchase of personal property without and its sale within the United States, shall be treated as derived entirely from sources within the country in which sold, * * *."

[4] In 1947 the Bureau of Internal Revenue in G. C. M. 25131, 1947-2 Cum. Bull. 85, acceded to the "title passage" test as universally adopted by the courts, and revoked G. C. M. 8594, IX-2 Cum. Bull. 354 (1930), which had invoked a "place of contract" rule. Taxpayers here apparently do not claim reliance upon the latter ruling; nor would they have been entitled to rely upon it.

G. C. M. 25131, in addition to laying down the "passage of title" rule, provides in part as follows: "In any case in which the sales transaction is arranged in a particular manner for the primary purpose of tax avoidance, the foregoing rules will not be applied. (See *Kaspare Cohn, Inc.* v. *Commissioner*, 35 B. T. A. 646). In such cases, all factors of the transaction, such as negotiations, the execution of the agreement, the location of the property, and the place of payment, will be considered, and the sale will be treated as having been consummated at the place where the substance of the sale occurred."

Here, by deliberate act of the parties, title, or at least beneficial ownership, passed to IAPI in the United States. Under the letters of credit, Balanovski was paid in the United States and CADIC's last act to complete performance was done here. When Balanovski presented evidence of shipment—the clean ocean bill of lading made out to the account of an Argentine bank with the directive "Notify IAPI"—he had completed CADIC's work and he received the final 1 per cent of IAPI's contract price.

The time when title to goods passes depends, of course, upon the intention of the parties. *Amtorg Trading Corp.* v. *Higgins, supra,* 2 Cir., 150 F. 2d 536; 1 Williston on Sales §259 (Rev. Ed. 1948); Uniform Sales Act §18; N. Y. Pers. Prop. Law §99. When documents of title, such as a bill of lading, are given up, the presumption is that the seller has given up title, together with the documents. See N. Y. Pers. Prop. Law §§115, 156, 219; 2 Williston on Sales §405 (Rev. Ed. 1948). In F.O.B. and F.A.S. contracts there is a presumption that title passes from the seller just as soon as the goods are delivered to the carrier "free on board" or "free alongside" the ship, as the case may be. See *Amtorg Trading Corp.* v. *Higgins, supra,* 2 Cir., 150 F. 2d 536; *Standard Casing Co.* v. *California Casing Co.,* 233 N. Y. 413, 135 N. E. 834; *Nelson Bros. Coal Co.* v. *Perryman-Burns Coal Co.,* 2 Cir., 48 F. 2d 99; 2 Williston on Sales §§280b, 280h (Rev. Ed. 1948); N. Y. Pers. Prop. Law §100, Rule 5. Both of these presumptions, which would tend to establish that title passed from CADIC to IAPI in the United States, are not altered by the use of a letter of credit. See *Briskey Co., supra,* 29 B. T. A. 987, 991, affirmed *C. I. R.* v. *Briskey Co.,* 3 Cir., 78 F. 2d 816. Nor need we here consider whether more than "beneficial" title passed immediately to IAPI or whether a "security" or "legal" title rested with the intermediary bank. See McCurdy, *Commercial Letters of Credit,* 35 Harv. L. Rev. 715, 736; Thayer, *C. I. F. Contracts in International Commerce,* 53 Harv. L. Rev. 792, 821.

All the available evidence confirms, rather than rebuts, these presumptions of passage of title in the United States.

All risk of loss passed before the ocean voyage. IAPI took out the marine insurance. CADIC performed all acts to complete the transaction, retained no control of the goods, and there was no possibility of withdrawal.

Judge Palmieri apparently did not contest that title to the goods passed in the United States. But he applied a test based upon the "substance of the transaction" to hold that Argentina was the place where the income-producing contracts were negotiated and concluded, the place of the buyer's business, and the destination of the goods. This led him to conclude that Argentina, rather than the United States, was the place of sale. The judge further buttressed this result by observing that IAPI, rather than CADIC, had insisted upon the passing of title in the United States.

Although the "passage of title" rule may be subject to criticism on the grounds that it may impose inequitable tax burdens upon taxpayers engaged in substantially similar transactions, such as upon exporters whose customers require that property in the goods pass in the United States—see Hearings before the House Committee on Ways and Means on Forty Topics Pertaining to the General Revision of the Internal Revenue Code, 83d Cong., 1st Sess., pt. 2, at 1458 (1953)—no suitable substitute test providing an adequate degree of certainty for taxpayers has been proposed. Vague "contacts" or "substance of the transaction" criteria would make it more difficult for corporations engaged in Western Hemisphere trade to plan their operations so as to receive the special deduction granted them if they derive at least 95 per cent of their income from sources outside the United States. Int. Rev. Code of 1954, §§921, 922; see also §941. See Note, *supra,* 69 Harv. L. Rev. 567.

Careful study was given this problem by the experts working on the Income Tax Project of the American Law Institute. They did give consideration to an alternative test of "place of destination." But this was open to criticism on the ground that it unduly favored exporters. See Surrey & Warren, *The Income Tax Project of the American Law Institute,* 66 Harv. L. Rev. 1161, 1196-1198. After

much deliberation the American Law Institute has retained the "title passage" rule in its 1954 draft of a model Internal Revenue Code. See American Law Institute, Federal Income Tax Statute, February 1954 Draft, vol. 2, §X906(c), and see comment at p. 483. Further, in substantially re-enacting §119(e)(2) of the 1939 Code, Congress did not further define "the place of sale," thus apparently accepting the prevailing "passage of title" test. See Int. Rev. Code of 1954, §§861(a)(6), 862(a)(6).

Of course this test may present problems, as where passage of title is formally delayed to avoid taxes.[5] Hence it is not necessary, nor is it desirable, to require rigid adherence to this test under all circumstances. But the rule does provide for a certainty and ease of application desirable in international trade.[6] Where, as here, it appears to accord with the economic realities (since these profits flowed from transactions engineered in major part within the United States), we see no reason to depart from it.[7] Hence we hold that the partners are liable for taxes on the entire profits of the partnership sales amounting to $7,763,702.20.

On the appeal of the defendant taxpayers the decision below is affirmed. On the appeal of the United States of America the judgment of the district court is reversed and the action is remanded for the entry of a judgment of recovery based upon a computation of taxes due in accordance with this opinion.

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[5] See Dean & Leake, *How To Arrange Foreign Sales So Title Will Pass "Outside the U. S." for Tax Purposes*, 94 J. Accountancy 457.

[6] Treas. Reg. 111, §29.119-8, promulgated under §119(e) of the Internal Revenue Code of 1939, provides that "the 'country in which sold' ordinarily means the place where the property is marketed."

The meaning of this definition is obscure, but surely we cannot construe it to mean the place of ultimate destination of the goods. Not only would such a construction be at variance with the decided cases, but it would make avoidance of American taxes not only simple but practically automatic.

[7] For discussions supporting the view taken in this opinion, see Note, 69 Harv. L. Rev. 567; 3 J. Taxation 43. On the general aspects of the problem, see 3 J. Taxation 113; 5 J. Taxation 111.

Appendix C.

UNITED STATES COURT OF APPEALS,

FOR THE SECOND CIRCUIT.

At a Stated Term of the United States Court of Appeals, in and for the Second Circuit, held at the United States Courthouse in the City of New York, on the 14th day of August, one thousand nine hundred and fifty-six.

Present:

Hon. CHARLES E. CLARK,
Chief Judge,

Hon. CARROLL C. HINCKS,

Hon. STERRY R. WATERMAN,
Circuit Judges.

UNITED STATES OF AMERICA,
Plaintiff-Appellant,

v.

ISRAEL BALANOVSKI, SAMUEL BERNARDO HORENSTEIN, etc.,
Defendants-Appellants,

ALICE DEVINE, BROWN BROS. HARRIMAN & CO. & MARINE MIDLAND TRUST COMPANY OF NEW YORK,
Defendants.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

On consideration whereof, it is now hereby ordered, adjudged, and decreed that the judgment of said District Court be and it hereby is affirmed on the appeal of the defendant taxpayers; and that the judgment of said District Court be and it hereby is reversed on the appeal of the United States and the action is remanded in accordance with the opinion of this Court.

A. Daniel Fusaro,
Clerk.

Appendix D.

G. C. M. 8594, IX-2 Cum. Bull. 354

SECTION 217.—NET INCOME OF NONRESIDENT ALIEN INDIVIDUALS.

ARTICLE 323: Sale of personal property. IX-44-4819
G. C. M. 8594

REVENUE ACTS OF 1913, 1916, 1917, AND 1918.

The taxpayer was a copartnership organized under German laws and having its principal place of business in South America. Its practice was for its principal office to cable the quantity and prices of hides and wool offered for sale to its representative in the United States, by whom these offers would be submitted to prospective buyers in the United States. Bids received were cabled to the principal office by its representative, who, upon receipt of cable acceptance, sent a letter to the purchaser confirming the sale on account of the taxpayer.

The place of the sales described and the source of the income therefrom were the United States. The entire net income of all business carried on in the United States by the taxpayer was taxable under the Revenue Act of 1913. The entire net income received from all sources within the United States was taxable under the Revenue Acts of 1916, 1917, and 1918.

The case of *Compañia General de Tabacos de Filipinas* v. *Collector* (279 U. S., 306) is conclusive that for determining the place of sale in deciding the source of income the substance of the sale is the agreement to sell.

General Counsel's Memorandum 2467 (C. B. VII-2, 188) and all other memoranda of the General Counsel inconsistent herewith are modified or revoked.

Recommended that Office Decision 1100 (C. B. 5, 118); I. T. 1569 (C. B. II-1, 126); I. T. 2068 (C. B. III-2, 164) be modified or revoked.

An opinion is requested whether certain transactions of the M Company gave rise to income from sources within the United States within the meaning of the Revenue Acts of 1913, 1916, 1917, and 1918.

The M Company, a copartnership organized under German law, had its principal place of business in South America, and branch offices in many countries, among which were branches in the cities of S and T, located in this country. The copartnership, under the Trading with the Enemy Act, applied in 1917 to the War Trade Board for a license to do business. It therein stated that it had in the city of S a manager and two salesmen and in the city of T a manager. It described its import business as consisting "of importing South American wool and hides for manufacturers and dealers located in this country. The bulk of these transactions was on buying orders for direct shipment to the purchasers against 90-day banker's letters of credit." In a letter written by A (who was at one time the city of S manager of the M Company) it is stated as follows:

> My duties consisted of keeping the M Company informed of market conditions, to sell wool and hides for their account in the United States and Canada, and to buy any goods they ordered for export, until the arrival of B in 1916, when he took the export end off my hands.
>
> A typical transaction of the import business into the United States would take place as follows: I would receive a cable from the M Company offering a certain quantity of merchandise (hides or wool)

at a certain price. I would submit these offerings to the various clients and cable the highest price obtainable for whatever quantity the client chose to bid on. In reply to this I would receive a cable accepting or rejecting the proposition.

If the business was accepted, I would send a letter to the purchaser confirming the sale for account of the M Company.

The terms of payment were 90 days' drafts against confirmed letter of credit through a first-class banking house.

The client in his turn would cause his bank to open this letter of credit in favor of the M Company. Up to August, 1914, all these credits were invariably in pounds sterling on a London bank. From then on they were dollar credits on United States banks or bankers, even when opened through Canada, where a large part of the hide business was done.

The city of S manager of the copartnership, upon the receipt of a cable from the South American office of the copartnership, stating the quantity and price of the hides and wool offered for sale, would submit these quantities and prices to prospective buyers in the United States. The city of S manager would then receive a bid from prospective buyers of the highest price they were willing to pay for specified quantities. These bids the manager would transmit by cable to the South American office and upon receipt of a cable "accepting or rejecting the proposition" the city of S manager would "if the business was accepted * * * send a letter to the purchaser confirming the sale on account of the M Company."

Congress may, if it chooses, levy a tax upon all income derived by a nonresident from the United States. (*DeGanay* v. *Lederer*, 250 U. S. 376). The Revenue Act of 1913 lays a tax "upon the entire net income from all property owned, and of every business, trade, or profession carried on in the United States by persons residing elsewhere." (Section II-A, subdivision 1, made applicable to partnerships by

Section II-D, third paragraph.) (See also Section II-B.) The M Company was admittedly carrying on business in the United States during the taxable years 1913, 1914, and 1915, and accordingly the entire net income of all business carried on in the United States by it during such years, including, of course, that from transactions of the type here presented, is subject to tax as prescribed by the Revenue Act of 1913.

A somewhat different issue is presented under the Revenue Acts of 1916, 1917, and 1918. These Acts lay a tax "upon the entire net income received * * * from all sources within the United States by every individual, a nonresident alien." Section 1(a) of the Revenue Act of 1916, made applicable to copartnerships by section 8 of the Revenue Act of 1916, as amended by section 1204, Revenue Act of 1917, and section 213(c), Revenue Act of 1918, made applicable to copartnerships by section 218, Revenue Act of 1918.) Under these Acts the Attorney General of the United States has ruled that the entire profit made by a foreign corporation from the sale in the United States of merchandise produced or purchased outside the United States is taxable income "from sources within the United States." (Opinions of the Attorney General of January 21, 1924, 34 Ops. A. G., 93, and of November 3, 1920, 32 Ops. A. G. 336, accepted and applied by T. D. 3576, C. B. III-1, 211, and T. D. 3111, C. B. 4, 280; O. D. 651, C. B. 3, 265.) The Board of Tax Appeals has taken the same view. (*Birkin* v. *Commissioner*, 5 B. T. A., 402; *Appeal of Yokohama Ki-Ito Kwaisha, Ltd.*, 5 B. T. A., 1248.) (See also Regulations 45, article 91.)

Whether the income from the transactions here under consideration is from sources within the United States is, therefore, determinable by whether the sales occurred in the United States.

The purpose and result of every sale of goods is to transfer the property in them from the seller to the buyer. At least so far as commercial transactions are concerned, this is effected by a bargain, agreement, or contract between the seller and the buyer. This contract may itself transfer

the property in the goods from seller to buyer, but unless the goods at the time of the contract are in being, and at the time specific and ascertained, the contract itself will not transfer the property in the goods, and, even though the goods are in being and specific and ascertained at the time of the contract, the contract will not transfer the property unless it manifests an intention so to do.

The term "sale" in both ordinary and legal speech is used indifferently; sometimes to describe the sum of the acts which begin with the making of a contract and end only with the final act of performance of that contract, at other times to describe the bargain or contract whereby the seller transfers or agrees to transfer the property, and at other times to describe the transfer of property in the goods from a seller to a buyer, or the event or act upon the doing or occurrence of which the property in the goods passes from seller to buyer. Where some of the acts or events, all of which are sometimes called the sale and at other times one or several of which are sometimes called the sale, occur at geographically distant places, the problem arises of determining at precisely which place the sale occurs. The law is necessarily forced to choose one of the acts or events involved in the sale and describe it as the sale, and the place of its occurrence as the place of sale.

Hence, there is considerable diversity in the judicial decisions respecting what is the sale, and accordingly respecting what is the place of sale. The only reconciling principle to be deduced from the decisions is that the act or event having the most cogent relationship to the legal issue presented for resolution in a particular field is deemed the sale, and the place where that act or event occurs is deemed the place of sale. Thus, in the field of constitutional law, where the jurisdiction of the United States or of one of its constituent States is in question, the substance of the sale is deemed the contract between the seller and buyer under which the property in the goods is either presently or ultimately transferred. Thus in *Norfolk & Western Railway Co.* v. *Sims* (191 U. S., 441, 447) the Supreme Court of the United States said:

> A sale really consists of two separate and distinct elements: first, a contract of sale, which is completed when the offer is made and accepted; and, second, a delivery of the property, which may precede, be accompanied by, or follow the payment of the price, as may have been agreed upon between the parties. The substance of the sale is the agreement to sell and its acceptance. * * *

In that case the court held that the bargain is made and the contract of sale completed as such when the contract to sell is made, even though the property in the goods is not transferred until after shipment, delivery, and payment. (See also *Robbins* v. *Shelby County Taxing District*, 120 U. S., 489; *Asher* v. *Texas*, 128 U. S., 129; *Brennan* v. *Titusville*, 153 U. S., 289; *Caldwell* v. *North Carolina*, 187 U. S., 622; *Dozier* v. *Alabama*, 218 U. S., 124; *Crenshaw* v. *Arkansas*, 227 U. S., 389.) Again, in *Rearick* v. *Pennsylvania* (203 U. S., 507, 512), the Supreme Court said:

> "Commerce among the several states" is a practical conception not drawn from the "witty diversities" ([*Yaites* v. *Gough*] Yelv., 33) of the law of sales. (*Swift & Co.* v. *United States*, 196 U. S., 375, 398, 399). The brooms were specifically appropriated to specific contracts, in a practical, if not in a technical, sense. * * *

In determining the nature of a sale and its relation to the jurisdiction of the Federal Government, or of one of the constituent States, the courts look to the essential character of the transaction rather than to its incidents. (*Western Union Tel. Co.* v. *Foster*, 247 U. S., 105; *Texas & New Orleans Railroad Co.* v. *Sabine Train Co.*, 227 U. S., 111.) As respects a sale of goods, technical rules as to the passing of title and the assumption of risk have no bearing in determining the jurisdictional question. (*American Express Co.* v. *Iowa*, 196 U. S., 133.) (See also *Superior Oil Co.* v. *Mississippi*, 50 S. Ct., 169.)

On the other hand, the word "sale" is frequently, particularly in the law of sales, used to describe "the transfer of property from one person to another for a consideration of value." (*Arnold* v. *North American Chemical Co.*, 232 Mass., 196, 122 N. E., 283.) (Sales act, section 1(2); cf. section 1, English sale of goods act.) In *Wheeler Lumber Bridge & Supply Co. of Des Moines, Iowa* v. *United States* (50 S. Ct., 419) the Supreme Court used the word in this latter sense. For a collection of cases using the word as meaning the contract, see *Williamson et al.* v. *Berry* (8 How., 495, 544), and for collection of cases using the word in both and various other meanings see note, 44 L. R. A. (N. S.), page 437.

In determining the source of income from the sale of goods, the question is presented whether the essential character of the transaction is decisive, or whether the technical rules as to the passing of the property in the goods and the assumption of risk are decisive.

This issue was presented to the Supreme Court of the United States in *Compañia General de Tabacos de Filipinas* v. *Collector* (279 U. S., 306), under section 10, Philippine income tax law, in every substantial particular the same as the corresponding provisions of the Revenue Act of 1916, Revenue Act of 1917, and Revenue Act of 1918. The case was presented on a stipulation reciting that the merchandise "was sold in the United States by the agency therein of the plaintiff's Philippine branch, the sale being subject to confirmation and absolute control as to price and other terms and conditions thereof, by the plaintiff's Philippine branch." The court said:

> While the stipulation states that the merchandise was "sold" in the United States by petitioner's agency there, this statement can not be taken without qualification; it must be read with the limitation immediately following, that such sales were "subject to confirmation and absolute control as to price and other terms and conditions" by petitioner's Philippine branch. It does not appear whether the confir-

mation was, in each case, given by the Philippine branch direct to the buyer or was otherwise the final act consummating the sales within the Philippine Islands, or whether, as the trial court and petitioner seem to have assumed, it was a mere approval or ratification of the negotiations had by petitioner's American agent, and authority to him to confirm or otherwise complete the sales in the United States. Certainly, if the former, the final acts of petitioner making effective the sales, which were the source of the profit, took place in the Philippine Islands as an incident to and part of its business conducted there. (See *Holder* v. *Aultman,* 169 U. S., 81, 89; *Lloyd Thomas Co.* v. *Grosvenor,* 144 Tenn., 349; *Charles A. Stickney Co.* v. *Lynch,* 163 Wis., 353; *Shuenfeldt* v. *Junkermann,* 20 Fed., 357.)

If, in fact, the sales were thus made in the Philippine Islands, we think it unimportant whether the merchandise sold was exported before or after its sale; it could not be seriously contended, and indeed petitioner does not contend, that a profit derived from such transactions would not be subject to the tax. For, in such a case, the entire transaction resulting in a profit, with the exception of the negotiations in the United States preceding the sale, would have taken place in the Philippines. Instead, petitioner asks us to construe the stipulation so as to bring it within the ruling of the Attorney General applied to a state of facts where every act effecting the sale took place outside the taxing jurisdiction. The ambiguous phraseology of the stipulation failing to disclose precisely how the business was done, we may not speculate as to its actual character. (See *Cochran* v. *United States,* 254 U. S., 387, 393.)

The decision is conclusive that the technical rules as to the passing of the property in the goods and the assumption of risk are not determinative of the place of sale and the source of income from the sale of goods. The essential

character of the transaction—the contract of sale—is the decisive factor in determining the place of sale for the purpose of determining the source of income. This is made clear by, first, the unequivocal statement of the court that the place where the goods are when the property in them is transferred is immaterial, the court saying "If, in fact, the sales were thus made in the Philippine Islands, we think it unimportant whether the merchandise sold was exported before or after its sale;" second, the language used by the court is appropriate only to the contractual phase of a sale, not to the property passing phase. Thus, "confirmation and absolute control as to price and other terms and conditions," "whether the confirmation was, in each case, given by the Philippine branch direct to the buyer or was otherwise the final act consummating the sales within the Philippine Islands, or whether * * * it was a mere approval or ratification of the negotiations had by petitioner's American agent, and authority to him to confirm or otherwise complete the sales in the United States" and "the final acts of petitioner making effective the sales" contemplate the process of contracting in respect of transferring the property in goods, not the process of actually transferring the property in goods; third, the conclusion of the court is immediately followed by specific reference to four cases, none of which concerns in the least the actual transfer of property in goods, but each of which concerns the making of a contract and the place where the acts requisite to the formation of a contract occur (express distinction being taken between the place where the contract is made and the place where it is to be performed), two of the cases involving contracts for the transfer in the future of the property in goods and expressly distinguishing between the contractual phase, and determining that the contractual phase is the decisive one. *Compañia General de Tabacos de Filipinas* v. *Collector* is therefore conclusive that, for the purpose of determining the place of sale so far as this is decisive of the source of income, "the substance of the sale is the agreement to sell." (*Norfolk & Western Railway Co.* v. *Sims*, 191 U. S. 441, 447.)

The rulings published as I. T. 1569, G. C. M. 2467, O. D. 1100, and I. T. 2068, being inconsistent with this decision of the Supreme Court, require modification or reversal.

In the instant case, the course of business is for the representative of the M Company in the United States to offer merchandise at certain prices to prospective buyers. The buyers thereupon designate to the representative of the M Company within the United States the goods, and the prices at which, they are willing to buy. The quantities and prices thus designated by the prospective buyer to the representative of the M Company constitute offers to buy. The representative of the M Company thereupon cables this information to the South American headquarters of his firm, and they cable back to the representative (not to the prospective buyer who is the offeror) their acceptance or rejection of the offer. Only when the representative in the United States of the M Company transmits to the prospective buyer the firm's acceptance is there any acceptance or any contract. When and where he transmits the "letter to the purchaser confirming the sale for account of the M Company," a contract of sale is there and then made, and it is under and in performance of that contract that the property in the goods is tranferred. No communication or transmittal of an acceptance by the M Company to their agent in the United States could constitute an acceptance of any offer made by an American buyer, and, therefore, at the most, the contract or contracts were made within the United States.

The sales in the instant case are therefore the substantial equivalent of the second alternative stated by the court in *Compañia General de Tabacos de Filipinas* v. *Collector*, namely, the sales being "subject to confirmation and absolute control as to price and other terms and conditions" by the seller's South American office, "the confirmation was, in each case, * * * a mere approval or ratification of the negotiations had by * * * [the seller's] American agent, and authority to him to confirm or otherwise complete the sales in the United States." Thus, in the instant case, the final acts of the seller incident to the sales, the final acts

making effective the sales, and the confirmation or completion of the sales, occurred in the United States, and, accordingly, it is the opinion of this office that, under the circumstances of this case, the place of the sales and the source of the income from the sales were the United States.

In view of the foregoing, General Counsel's Memorandum 2467 and all other memoranda of this office inconsistent herewith are modified or revoked. It is recommended that O. D. 1100, I. T. 1569, and I. T. 2068 be modified or revoked.

C. M. CHAREST,
General Counsel, Bureau of Internal Revenue.

Appendix E.

G. C. M. 25131, 1947-2 Cum. Bull. 85

SECTION 119.—INCOME FROM SOURCES WITHIN UNITED STATES.

SECTION 29.119-8: Sale of personal property.

1947-22-12674
G. C. M. 25131

INTERNAL REVENUE CODE AND PRIOR REVENUE LAWS.

As a general rule, for the purpose of determining the source of income attributable to the sale of personal property, a sale is consummated at the place where the seller surrenders all his right, title, and interest to the buyer. Where bare legal title is retained by the seller, the sale will be deemed to have occurred at the time and place of passage to the buyer of beneficial ownership and risk of loss.

Where the sales transaction is arranged for the primary purpose of tax avoidance, the foregoing rules will not be applied. In such cases, all factors of the transaction, such as negotiations, execution of the agreement, location of the property, and place of payment, will be considered, and the sale will be treated as having been consummated at the place where the substance of the sale occurred.

G. C. M. 8594 (C. B. IX-2, 354 (1930)) revoked, and G. C. M. 13475 (C. B. XIII-2, 224 (1934)) modified. Recommended that I. T. 2549 (C. B. IX-2, 360 (1930)) be revoked and that I. T. 2806 (C. B. XIII-2, 78 (1934)) be modified.

In view of acquiescence (page 2, this Bulletin) by the Commissioner in *East Coast Oil Co., S. A.*, v. *Commissioner* (31 B. T. A., 558); reconsideration has been given to G. C. M. 8594 (C. B. IX-2, 354 (1930)), which holds that the place of execution of a contract of sale is the decisive factor in determining the place of sale and, hence, in determining whether the source of income resulting from such a contract is within or without the United States. Adoption of that rule was accompanied by a reversal (I. T. 2549, C. B. IX-2, 360 (1930)) of the long-standing position of the Bureau that, generally, in a sales transaction, the place where title passes determines the source of income. The conclusion reached in G. C. M. 8594, *supra*, was based in part on the opinion in *Compania General de Tabacos de Filipinas* v. *Collector* (279 U. S., 306), certain parts of which were deemed to be susceptible of an interpretation that the place where a contract of sale is entered into is the decisive factor in determining the place of sale and thus the source of income. In *East Coast Oil Co., S. A.*, v. *Commissioner, supra* (affirmed, 85 Fed. (2d), 322, certiorari denied, 299 U. S., 608), the Board stated in part as follows:

> As we read it, the Compania General case in no wise varies the established rule that the place where title passes is the place of sale. There a tax (arising under provisions of the Philippine income tax law similar to the provisions of the 1918 and 1921 Acts here material) was imposed upon net income received from sources within the Philippine Islands.
>
> The taxpayer plaintiff was a corporation which produced and purchased products within the Islands and disposed of them in the United States through a branch agency. Under the law, the profits on the sales were subject to the Philippine tax, unless the sales were made in the United States. The case was submitted to the Court upon a stipulation to the effect that the sales were made in the United States, subject however to final confirmation by the plaintiff

in the Philippines. Under that stipulation the Court could not but conclude that when confirmation was given, the sale became complete, and that it was not complete until confirmation was given. The stipulation was consistent only with the proposition that property in the goods passed, *co instanti,* upon the confirmation made in the Philippines—that the place of sale is where the final act of the seller, causing title to pass, was done. And to that effect was respondent's argument to the Court. The Court did not say that the place where is made an executory contract of sale is necessarily the place of sale; it did not set aside the rule that a sale is consummated when and where the property in the goods passes. (See Briskey Co., 29 B. T. A., 987 [acquiescence, page 1, this Bulletin].)

See also *Ronrico Corporation* v. *Commissioner* (44 B. T. A., 1130, acquiescence, C. B. 1944, 24) and *The Exolon Co.* v. *Commissioner* (45 B. T. A., 844, acquiescence, page 1, this Bulletin).

In view of the foregoing, this office adopts the general rule that, for the purpose of determining the source of income attributable to the sale of personal property, a sale is consummated at the place where the seller surrenders all his right, title, and interest to the buyer. In cases in which the bare legal title is retained by the seller, the sale will be deemed to have occurred at the time and place of the passage to the buyer of the beneficial ownership and the risk of loss. (See *Ronrico Corporation* v. *Commissioner, supra.*) However, in any case in which the sales transaction is arranged in a particular manner for the primary purpose of tax avoidance, the foregoing rules will not be applied. (See *Kaspare Cohn, Inc.* v. *Commissioner,* 35 B. T. A., 646.) In such cases, all factors of the transaction, such as negotiations, the execution of the agreement, the location of the property, and the place of payment, will be considered, and the sale will be treated as having been

consummated at the place where the substance of the sale occurred.

G. C. M. 8594, *supra,* is revoked, and G. C. M. 13475 (C. B. XIII-2, 224 (1934)) is modified to the extent it is inconsistent herewith. It is recommended that I. T. 2549, *supra,* be revoked, and that I. T. 2806 (C. B. XIII-2, 78 (1934)) be modified to the extent it is inconsistent herewith.

J. P. WENCHEL,
Chief Counsel, Bureau of Internal Revenue.

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In the Supreme Court of the United States

OCTOBER TERM, 1956

No. 560

ISRAEL BALANOVSKI, SAMUEL BERNARDO HORENSTEIN, COMPANIA ARGENTINA DE INTERCAMBIO COMERCIAL, I. BALANOVSKI & CIA (SOMETIMES CALLED "CADIC"), A CO-PARTNERSHIP, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinions of the District Court (R. 6–26)[1] are reported at 131 F. Supp. 898. The opinion of the Court of Appeals (Pet. App. 4a–17a) is reported at 236 F. 2d 298.

JURISDICTION

The judgment of the Court of Appeals (Pet. App. 18a–19a) was entered on August 14, 1956. The petition for a writ of certiorari was filed on November

[1] Record references are to the appendix to appellant's brief in the Court of Appeals.

9, 1956. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254.

QUESTIONS PRESENTED

1. Whether the court below erred in affirming the District Court's determination that it had jurisdiction to render a personal judgment against the taxpayers, nonresident alien members of a partnership, where (*a*) the court acquired jurisdiction *in rem* over taxpayers' funds located in the United States and taxpayers appeared and defended on the merits; and (*b*) process was served on an authorized agent of taxpayers.

2. Whether the court below erred in holding that the partnership's purchasing and selling and related activities in the United States amounted to engaging in a business within the purview of Sections 211 (b), 212 (a) and 219 of the Internal Revenue Code of 1939, and that consequently taxpayers as co-partners were taxable not merely on a portion of the income derived from such activities (as the District Court held) but on all of the partnership profits derived from the business.

STATUTE AND OTHER AUTHORITIES INVOLVED

The statutes involved are Sections 119 (a) and (e), 181, 182 (c), 211 (b), 212 (a), 219, 3670, and 3678 (a) of the Internal Revenue Code of 1939. These and Sections 29.51–2 and 29.217–2 (a) and (b) of Treasury Regulations 111 and Rule 4 (d) (1) of the Federal Rules of Civil Procedure are printed in the Appendix, *infra*, pp. 18–22.

STATEMENT

The material facts as stipulated (R. 42–52) and found by the District Court (R. 6–8) are set out in the opinion below (Pet. App. 5a–9a) as follows:[2]

Taxpayers Balanovski and Horenstein were co-partners in the Argentine partnership, Compania Argentina de Intercambio Comercial (CADIC), Balanovski having an 80 per cent interest and Horenstein a 20 per cent interest. Balanovski, an Argentinian citizen, came to the United States on or about December 20, 1946, and remained in this country for approximately ten months, except for an absence of a few weeks in the spring of 1947 when he returned to Argentina. While here, he made extensive purchases and sales of trucks and other equipment on behalf of the partnership, resulting in a profit to the partnership of some $7,763,702.20.

His usual mode of operation in the United States was to contact American suppliers and obtain offers for the sale of equipment. He then communicated the offers to his father-in-law, Horenstein, in Argentina. Horenstein, in turn, submitted them at a markup to an agency of the Argentine Government, Instituto Argentino de Promocion del Intercambio (IAPI), which was interested in purchasing such equipment. If IAPI accepted an offer, Horenstein would notify Balanovski and the latter would accept the corresponding original offer of the American supplier. In

[2] Some of the facts set out in the opinion below, while not contained in the stipulation or the District Court's opinion, are based upon the uncontradicted testimony of taxpayers' witnesses and are undisputed.

the meantime IAPI would cause a letter of credit in favor of Balanovski to be opened with a New York bank. Acting under the terms of the letter of credit Balanovski would assign a portion of it, equal to CADIC's purchase price, to the United States supplier. The supplier could then draw on the New York bank against the letter of credit by sight draft for 100 per cent invoice value accompanied by (1) a commercial invoice billing Balanovski, (2) an inspection certificate, (3) a nonnegotiable warehouse or dock receipt issued in the name of the New York bank for the account of IAPI's Argentine agent, and (4) an insurance policy covering all risks to the merchandise up to delivery F. O. B. New York City. Then, if the purchase was one on which CADIC was to receive a so-called quantity discount or commission, the supplier would pay Balanovski the amount of the discount. These discounts, paid after delivery of the goods and full payment to the suppliers, amounted to $858,595.90, constituting funds which were delivered in the United States.

After the supplier had received payment, Balanovski would draw on the New York bank for the unassigned portion of the letter of credit, less one per cent of the face amount, by submitting a sight draft accompanied by (1) a commercial invoice billing IAPI, (2) an undertaking to ship before a certain date, and (3) an insurance policy covering all risks to the merchandise up to delivery F. A. S. United States Sea Port. The bank would then deliver the nonnegotiable warehouse receipt that it had received from the supplier to Balanovski on trust receipt and his under-

taking to deliver a full set of shipping documents, including a clean on board bill of lading issued to the order of IAPI's Argentine agent, with instructions to notify IAPI. It would also notify the warehouse that Balanovski was authorized to withdraw the merchandise. Upon delivery of these shipping documents to the New York bank Balanovski would receive the remaining one per cent due under the terms of the letter of credit. Although Balanovski arranged for shipping the goods to Argentina, IAPI paid shipping expenses and made its own arrangement there for marine insurance. The New York bank would forward the bill of lading, Balanovski's invoice billing IAPI, and the other documents required by the letter of credit (not including the supplier's invoice billing Balanovski) to IAPI's agent in Argentina.

Twenty-four transactions following substantially this pattern took place during 1947. Other transactions were also effected which conformed to a substantially similar pattern, except that CADIC engaged the services of others to facilitate the acquisition of goods and their shipment to Argentina. And other offers were sent to Argentina, for which no letters of credit were opened. Several letters of credit were opened which remained either in whole or in part unused. In every instance of a completed transaction Balanovski was paid American money in New York, and in every instance he deposited it in his own name with New York banks. Balanovski never ordered material from a supplier for which he did not have an order and letter of credit from IAPI.

Balanovski's activities on behalf of CADIC in the United States were numerous and varied and required the exercise of initiative, judgment, and executive responsibility. They far transcended the routine or merely clerical. Thus he conferred and bargained with American bankers. He inspected goods and made trips out of New York State in order to buy and inspect the equipment in which he was trading. He made sure the goods were placed in warehouses and aboard ship. He tried to insure that CADIC would not repeat the errors in supplying inferior equipment that had been made by some of its competitors. And while here he attempted "to develop" "other business" for CADIC.

Throughout his stay in the United States Balonovski employed a Miss Alice Devine as a secretary. She used, and he used, the Hotel New Weston in New York City as an office. His address on the documents involved in the transactions was given as the Hotel New Weston. His supplier contacted him there, and that was the place where his letters were typed and his business appointments arranged and kept. Later Miss Devine opened an office on Rector Street in New York City, which he also used. When he returned to Argentina for a brief time in 1947 he left a power of attorney with Miss Devine. This gave her wide latitude in arranging for shipment of goods and in signing his name to all sorts of documents, including checks. When he left for Argentina again at the end

of his 10-month stay, he left with Miss Devine the same power of attorney,[3] which she used throughout the balance of 1947 to arrange for and complete the shipment of goods and bank the profits.

When Balanovski left the United States in October 1947 he filed a departing alien income tax return, on which he reported no income. In March 1948 the Commissioner of Internal Revenue assessed $2,122,393.91 as taxes due on income for the period during which Balanovski was in the United States. In May 1953 the Commissioner made a jeopardy assessment against Balanovski in the amount of $3,954,422.41 and gave him notice of it. At the same time a similar jeopardy assessment, followed by a timely notice of deficiency, was made against Horenstein in the amount of $1,672,209.90, representing his alleged share of CADIC's profits on the above-described sales of United States goods.

The Government brought the present action to foreclose a federal tax lien on $511,655.58 and $42,529.49—amounts of partnership funds held in two United

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[3] The power of attorney consisted of 13 paragraphs covering such topics as "Endorsement for Deposit," "Signing checks and settling accounts," "Acceptances," "Procuring Discounts," "Sale of securities," "Borrowing and giving security," "Letters of Credit," and "Contracts."

One of these paragraphs read as follows:

> (General authority and substitution)—Give unto said attorney(s) full power and authority to do and to perform every act whatsoever requisite and convenient to be done in the premises as fully as I might do if personally present with full power of substitution and revocation hereby ratifying all that my said attorney(s) or the substitute(s) shall do or cause to be done by virtue hereof; * * *.

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States banks—and to obtain personal judgments against Balanovski and Horenstein in the sums of $6,722,625.54 (subsequently reduced to $5,050,415.64) and $1.672,209.90 respectively. Balanovski and Horenstein were served with process by mail in Argentina pursuant to 28 U. S. C., Section 1655; and Miss Devine, the purported agent of Balanovski, was personally served in New York. Taxpayers then appeared by their attorneys and proceeded to defend the action.

The District Court held that it had jurisdiction *in rem,* and also that it had jurisdiction to render a judgment binding taxpayers personally. The Court of Appeals agreed. (Pet. App. 9a–11a.) On the merits, the District Court held that the partners were taxable on only a portion of the profits from the sales, i. e., on the discounts received by Balanovski from the American suppliers, but not on the balance. (R. 8–18.) The Court of Appeals disagreed, holding that the partners were taxable on all the sales profits received. (Pet. App. 11a–17a.)

ARGUMENT

1. The court below properly approved the District Court's holding that it acquired jurisdiction, both *in rem* and *in personam,* to determine taxpayers' tax liability. The *in rem* jurisdiction over the partnership funds held in United States banks (Pet. App. 8a–9a) rests upon Sections 3670 and 3678 (a) of the Internal Revenue Code of 1939 (Appendix, *infra,* pp. 20–21). Section 3670 vests in the United States a tax lien upon all property of a delinquent taxpayer, while Section 3678 (a) authorizes enforcement of the

lien by civil action. Taxpayers "question" (Pet. 13, fn. 1) whether the court had *in rem* jurisdiction, on the theory that the bank deposits belonged to the partnership and not to them individually as partners—a theory which disregards the basic statutory scheme for taxing income of members of a partnership. Partnerships are not separate entities for federal income tax purposes; the partners individually own the partnership property and are liable for tax only in their individual capacities. Sections 181, 182 and 219 of the Internal Revenue Code of 1939 (Appendix, *infra,* pp. 19, 20). See also New York Partnership Law, Sections 50–52. Far from departing from this elementary rule, the case upon which taxpayers rely in this connection (*United States* v. *Worley,* 213 F. 2d 509 (C. A. 6th), certiorari denied, 348 U. S. 917) confirms and applies it.

The court below also correctly sustained the District Court's holding that, since taxpayers appeared and defended on the merits, it had jurisdiction to render a judgment *in personam* for the amount of tax owing. It is true, as taxpayers assert (Pet. 7–13) and the court below recognized (Pet. App. 10a), that there is some diversity of opinion on this point. For the reasons stated by the court below (Pet. App. 10a), we submit that its ruling is eminently sound. The taxpayers have been fully heard on the merits of the issues determinative of their total tax liability; to limit jurisdiction to the funds found in the United States could lead only to superfluous litigation in the event additional funds are later found, since in any further

litigation to collect the balance owing, the taxpayers would again lose on the merits under principles of collateral estoppel or *stare decisis*. See 2 Moore's *Federal Practice*, Section 12.13 (2d ed., 1948).[4]

In any event, this case presents no need or occasion to resolve any alleged conflict as to whether the court had power to render a personal judgment against taxpayers. As the court below pointed out (Pet. App. 10a–11a), there is a separate and alternative basis for jurisdiction *in personam*, namely, the personal service of process made on taxpayer's agent, Miss Devine (Pet. App. 9a), pursuant to Rule 4 (d) (1) of the Federal Rules of Civil Procedure (Appendix, *infra*, p. 21).[5]

Under that Rule personal service may be effected upon "an agent authorized by appointment or by law" to receive services of process. The comprehensive power of attorney given to Miss Devine clearly warranted the conclusion that she was taxpayers' agent for service of process by virtue of an appointment in fact. Among other things, it gave her "*full* power and

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[4] Moreover, even if this Court were to reverse the courts below and hold that the District Court lacked jurisdiction to render a personal judgment, taxpayers would not as a practical matter derive any substantial present advantage. While the judgment exceeds the amount of the funds located in the United States (over which the court clearly had jurisdiction), it does not appear that there are any other assets which could be subjected to satisfaction of the judgment. Unless and until additional assets are found in the United States the question of validity of a personal judgment remains academic. And even in that event, another action *in rem* would lie to enforce the federal lien for the balance of tax owing.

[5] In addition, taxpayers were served by mail, pursuant to 28 U. S. C., Section 1655. (Pet. App. 9a.)

authority to do and to perform every act whatsoever requisite and convenient to be done in the premises as fully as I might do if *personally present* * * *" (Pet. App. 8a.) [Italics supplied.] As the court below observed (Pet. App. 11a) the power "was broad and sweeping in its terms, and an implied actual appointment to receive service of process may be readily spelled out therefrom".

Taxpayers contend that the authority to receive service must be "plainly specified" and that the agent must have "specific authority" (Pet. 12, 13), citing *Osterling* v. *Commonwealth Trust Co.*, 35 F. Supp. 704 (W. D. Pa.), affirmed *per curiam*, 115 F. 2d 809 (C. A. 3d). That case, however, does not go so far, but rather holds that on the facts presented there was no such authority. Other decisions, also holding that the determination is made on the particular facts, have found the requisite authority to exist on the basis of agency powers much narrower than those here given to Miss Devine. (*Cohen* v. *Physical Culture Shoe Co.*, 28 F. Supp. 679 (S. D. N. Y.); *Szabo* v. *Keeshin Motor Express Co.*, 10 F. R. D. 275 (N. D. Ohio). The question of whether the service was made upon a duly appointed "agent" is one on which there is no conflict among the circuits; it turns on the interpretation of a particular instrument, and raises no issue of general importance warranting the attention of this Court.

Even assuming, arguendo, that the courts below erred in concluding that the power of attorney granted to Miss Devine was broad enough to make her taxpayer's agent in fact to receive process on their behalf,

the conclusion is unescapable that she was their agent by operation of the federal income tax laws. Pursuant to the sweeping terms of the power of appointment, Miss Devine took charge of all transactions of the partnership after Balanovski's departure from the country, and obtained and banked its profits. Under the applicable Treasury Regulations[6] she was required as the agent of a nonresident alien subject to tax to file a federal income tax return and pay the tax on his behalf, and she in fact filed a return for the taxable year in which she described herself as "agent" for Balanovski. Since she was personally responsible for filing returns and paying taxes on the partnership income which actually flowed through her hands, and filed a return as agent, she and her principals are liable for taxes owing on that income. These circumstances, the court below properly noted (Pet. App. 11a), resulted in Miss Devine's "authorization by operation of law (in addition to her appointment in fact) to receive service of process" for taxpayers.

2. As for the merits, there is likewise no occasion for further review. The court below correctly held that the partnership of which taxpayers were the members was "engaged in trade or business in the United States", within the meaning of Section 211 (b) of the Internal Revenue Code of 1939 (Appendix, *infra*, p. 19), and that therefore taxpayers were taxable not only on some of the business profits (as the District

[6] Sections 29.217-2 and 29.51-2 of Treasury Regulations 111 (Appendix, *infra*, pp. 21-22).

Court had held), but on all of the profits. See also Sections 119 (e), 212 (a), and 219 (Appendix, *infra*, p. 18.[7] Whether the activities of the partnership amounted to the carrying on of a business in the United States presented a question of ultimate fact. Contrary to taxpayers' contention, the partnership was doing more than merely purchasing goods here for sale abroad. As the court below pointed out (Pet. App. 12a), it "was actively and extensively engaged in business in the United States in 1947", the taxable year. Balanovski, the 80 percent partner, lived in the United States for a period of about ten months of the year (except for a short absence), during which time he located suppliers, solicited orders, inspected merchandise, made numerous purchases, and resold the merchandise—resulting in partnership profits of almost $8,000,000. He maintained bank accounts in the United States for the partnership funds, and a New York office from which the major portion of the partnership business was transacted. And even after he left the country, the partnership continued through an agent (Miss Devine) to transact business here. On the basis of these evidentiary facts—which are undisputed—the court below was amply justified in holding that the partnership was engaged in business in the

[7] Under Sections 211 (b) and 212 (a), nonresident aliens engaged in business in the United States are taxable on income from sources within the United States, and under Section 219 a nonresident alien is considered as being engaged in business within the United States if a partnership of which he is a member is so engaged. Under Section 119 (e) profits from the sale of personal property within the United States are treated as income from sources within the United States.

United States. See, e. g., *Commissioner* v. *Nubar,* 185 F. 2d 584 (C. A. 4th), certiorari denied, 341 U. S. 925; *Pinchot* v. *Commissioner,* 113 F. 2d 718 (C. A. 2d); *Lewenhaupt* v. *Commissioner,* 20 T. C. 151. Cf., *Edwards* v. *Chile Copper Co.,* 270 U. S. 452, 455–456; *Deputy* v. *du Pont,* 308 U. S. 488, 499. Moreover, as the court below also pointed out (Pet. App. 13a–15a), quite apart from its other business activities the partnership "sold" goods in the United States, within the settled meaning of that term, since title or at least beneficial ownership passed to the purchasers and payment was made in the United States. See, e. g., *Commissioner* v. *East Coast Oil Co.,* 85 F. 2d 322 (C. A. 5th), certiorari denied, 299 U. S. 608; *Commissioner* v. *Briskey Co.,* 78 F. 2d 816 (C. A. 3d); *Ronrico Corp.* v. *Commissioner,* 44 B. T. A. 1130.

Taxpayers do not and cannot assert conflict with any other decision. Indeed, they make no attempt to distinguish the numerous decisions, with which the decision below is in accord, cited by the court below. (Pet. App. 12a, 14a.) The lone case mentioned by taxpayers in this connection (*Compania General* v. *Collector,* 279 U. S. 306) concededly (Pet. 17–18) does not involve the statutory provisions applicable here; and even if it were regarded as posing the same question, the decision below is fully consistent with that case, for it was there held that sales were made in the place (Philippine Islands) where the final acts making them effective occurred.

Nor does this case present an important question, as taxpayers claim. (Pet. 7, 13.) It turns on the application of settled principles to the particular facts

of this case. Relying upon a General Counsel Memorandum which was revoked in 1947 (G. C. M. 8594, IX-2 Cum. Bull. 354 (1930), revoked in G. C. M. 25131, 1947-2 Cum. Bull. 85), taxpayers contend (Pet. 13-17) that the criteria for determining where goods are sold are unsettled and should be clarified by this Court; and that the court below applied an erroneous test in fixing the place of sale as the place where title passes. However, the governing principles have been made abundantly clear by the numerous court decisions—both before and after 1947—cited and followed by the court below (Pet. App. 14a), applying the so-called "passage of title test". Furthermore, as is plain from its opinion, the court below reached its conclusion that the partnership was engaged in business in the United States, within the purview of Sections 211 (b) and 219, not only on the ground that it made sales in the United States, but on the basis of all the partnership business activities, including the sales.

What is more, in relying upon G. C. M. 8594, *supra,* taxpayers erroneously assume that the Commissioner was precluded from revoking that ruling. The Commissioner has statutory authority to determine the extent to which even a Treasury Regulation may be retroactively applied (1939 Code Section 3791 (b); *Helvering* v. *Reynolds Co.,* 306 U. S. 110, 116); *a fortiori,* he has such authority with respect to informal rulings like General Counsel Memoranda. The doctrine of implied legislative approval of the Treasury's interpretation of a statute, invoked by taxpayers (Pet. 21, 22), applies to formal Treasury

Regulations promulgated by the Secretary, not to informal administrative rulings. *Biddle* v. *Commissioner,* 302 U. S. 573, 582; *Helvering* v. *N. Y. Trust Co.,* 292 U. S. 455, 468. At any rate, there is no showing here that taxpayers were entitled to or did in fact rely on the prior ruling. On the contrary, they were placed on notice by the many court decisions (cited in the opinion below) uniformly rejecting that ruling as an erroneous interpretation of the statute. Indeed, the later ruling (G. C. M. 25131, *supra*) which replaced it and was followed by the court below was issued in deference to those decisions, and embodies the settled judicial interpretation.[8] There is little similarity between this case and *Automobile Club of Mich.* v. *Commissioner,* 230 F. 2d 585 (C. A. 6th), certiorari granted, 352 U. S. 817, October 8, 1956, which taxpayers cite in this connection. (Pet. 22.) That case, unlike this one, involved a specific

[8] In 1947 the Commissioner recognized that the courts had universally adopted the "title passage" test and accordingly G. C. M. 25131 replaced G. C. M. 8594. The earlier G. C. M. had adopted a "place of contract" test; but no court had followed that test, and the Bureau had in 1944 acquiesced to the *Ronrico* case, *supra* (1944 Cum. Bull. 24). Taxpayers cannot claim reliance upon the older rule, since the title page of the volume in which it was contained called special attention to the fact that the rulings do not have the effect of Treasury Decisions (Regulations) and do not commit the Treasury Department to any interpretation. Nor did taxpayers in fact rely upon the older ruling. $300,000 of the money levied upon stems from sales carried through by Balanovski in the way all others were carried out—upon the advice of counsel—after the Government had served notices of liens on the New York banks. (Appellee's Appendix in the Court of Appeals, 12a, 37a.)

ruling given to a particular taxpayer absolving it of tax liability for past years, not a general interpretative ruling.

CONCLUSION

This case turns on its own facts. It presents no conflict requiring resolution by this Court, and no other ground for further review. The petition for a writ of certiorari should be denied.

Respectfully submitted.

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DECEMBER 1956.

APPENDIX

Internal Revenue Code of 1939:

SEC. 119. INCOME FROM SOURCES WITHIN UNITED STATES.

(a) *Gross Income From Sources in United States.*—The following items of gross income shall be treated as income from sources within the United States:

* * * * *

(6) *Sale of Personal Property.*—

For gains, profits, and income from the sale of personal property, see subsection (e).

* * * * *

(e) *Income from Sources Partly Within and Partly Without United States.*—* * *

* * * * *

* * * Gains, profits and income derived from the purchase of personal property within and its sale without the United States or from the purchase of personal property without and its sale within the United States, shall be treated as derived entirely from sources within the country in which sold, except that gains, profits, and income derived from the purchase of personal property within a possession of the United States and its sale within the United States shall be treated as derived partly from sources within and partly from sources without the United States.

* * * * *

(26 U. S. C. 1952 ed., Sec. 119.)

SEC. 181. PARTNERSHIP NOT TAXABLE.

Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity.

(26 U. S. C. 1952 ed., Sec. 181.)

SEC. 182. TAX OF PARTNERS.

In computing the net income of each partner, he shall include, whether or not distribution is made to him—

* * * * *

(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183 (b).

(26 U. S. C. 1952 ed., Sec. 182.)

SEC. 211. TAX ON NONRESIDENT ALIEN INDIVIDUALS.

(b) [as amended by Sec. 160 (d), Revenue Act of 1942, c. 619, 56 Stat. 798] *United States Business or Office.*—A nonresident alien individual engaged in trade or business in the United States shall be taxable without regard to the provisions of subsection (a). As used in this section, section 119, section 143, section 144, and section 231, the phrase "engaged in trade or business within the United States" includes the performance of personal services within the United States at any time within the taxable year, but does not include the performance of personal services for a nonresident alien individual, foreign partnership, or foreign corporation, not engaged in trade or business within the United States, by a nonresident alien individual temporarily present in the United States for a period or periods not exceeding a total of ninety days during the taxable year and whose compensation for such services does not exceed in the aggregate $3,000. * * *

* * * * *

(26 U. S. C. 1952 ed., Sec. 211.)

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SEC. 212. GROSS INCOME.

(a) *General Rule.*—In the case of a nonresident alien individual gross income includes only the gross income from sources within the United States.

* * * * *

(26 U. S. C. 1952 ed., Sec. 212.)

SEC. 219 [as amended by Sec. 160 (f), Revenue Act of 1942, *supra*]. PARTNERSHIPS.

For the purpose of this chapter, a nonresident alien individual shall be considered as being engaged in a trade or business within the United States if the partnership of which he is a member is so engaged.

(26 U. S. C. 1952 ed., Sec. 219.)

SEC. 3670. PROPERTY SUBJECT TO LIEN.

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, penalty, additional amount, or addition to such tax, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.

(26 U. S. C. 1952 ed., Sec. 3670.)

SEC. 3678. CIVIL ACTION TO ENFORCE LIEN ON PROPERTY.

(a) *Filing.*—In any case where there has been a refusal or neglect to pay any tax, and it has become necessary to seize and sell property and rights to property, whether real or personal, to satisfy the same, whether distraint proceedings have been commenced or not, the Attorney General at the request of the Commissioner may direct a civil action to be filed, in a district court of the United States, to enforce the lien of the United States for tax upon any property and

rights to property, whether real or personal, or to subject any such property and rights to property owned by the delinquent, or in which he has any right, title, or interest, to the payment of such tax.

* * * * *

(26 U. S. C. 1952 ed., Sec. 3678.)

Federal Rules of Civil Procedure:

RULE 4. *Process.*

* * * * *

(d) *Summons: Personal Service.* The summons and complaint shall be served together. The plaintiff shall furnish the person making service with such copies as are necessary. Service shall be made as follows:

(1) Upon an individual other than an infant or an incompetent person, by delivering a copy of the summons and of the complaint to him personally or by leaving copies thereof at his dwelling house or usual place of abode with some person of suitable age and discretion then residing therein or by delivering a copy of the summons and of the complaint to an agent authorized by appointment or by law to receive service of process.

* * * * *

Treasury Regulations 111, promulgated under the Internal Revenue Code of 1939:

SEC. 29.51–2 [as amended by T. D. 5425, 1945 Cum. Bull. 10, and T. D. 5649, 1948–2 Cum. Bull. 57]. *Form of Return.*—(a) *Taxable years beginning before January 1, 1944.*—* * * * * * The return may also be made by an agent if the taxpayer is unable to make the return by reason of continuous absence from the United States for a period of at least 60 days prior to the date prescribed by law for making the return. Whenever a return is made by an agent it must be accompanied by

the prescribed power of attorney, Form 935, except that an agent holding a valid and subsisting general power of attorney authorizing him to represent his principal in making, executing, and filing the income return, may submit a certified copy thereof in lieu of the authorization on Form 935. The taxpayer and his agent, if any, are responsible for the return as made and incur liability for the penalties provided for erroneous, false, or fraudulent returns. For returns of nonresident aliens, see sections 29.217–1 and 29.217–2.

* * * * *

(b) *Taxable years beginning after December 31, 1943 and prior to January 1, 1948.*— (1) *General.*—* * * The provisions of subsection (a) of this section insofar as they apply to the time and manner of making a return on Form 1040 are equally applicable to taxable years beginning after December 31, 1943 and prior to January 1, 1948.

* * * * *

SEC. 29.217–2. *Return of Income.*—

* * * * *

(b) *United States business.*—

* * * * *

The responsible representative or agent within the United States of a nonresident alien individual who at any time within the taxable year was engaged in trade or business within the United States shall make in behalf of his nonresident alien principal, a return of, and shall pay the tax on, all income from sources within the United States coming within his control as representative or agent. The agency appointment will determine how completely the agent is substituted for the principal for tax purposes. * * *

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Supreme Court of the United States

OCTOBER TERM, 1956.

No. 560

ISRAEL BALANOVSKI, SAMUEL BERNARDO HORENSTEIN, COMPANIA ARGENTINA DE INTERCAMBIO COMERCIAL, I. BALANOVSKI & CIA. (sometimes called "CADIC"), a co-partnership,

Petitioners,

v.

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR REHEARING OF ORDER DENYING PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT.

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Petitioners,

against

UNITED STATES OF AMERICA,

Respondent.

PETITION FOR REHEARING OF ORDER DENYING PETITION FOR WRIT OF CERTIORARI.

Petitioners respectfully pray that this Court grant a rehearing of its order of January 14, 1957, denying the petition for writ of certiorari herein, and that a writ of certiorari be issued to review the judgment of the United States Court of Appeals for the Second Circuit, entered August 14, 1956, affirming in part and reversing in part a decision of the United States District Court for the Southern District of New York entered on June 23, 1955.

Reasons for Granting Rehearing and Issuing the Writ.

Preliminarily.

To sustain the judgment below, it was necessary for the Government to establish two propositions: (a) that CADIC, during the period in question, was engaged in business in the United States; and (b) that the monies in question were derived from sales of personal property within the United States or, as the Code phrases it (§119 (e), I. R. C. of 1939), "from sources within the country in which sold."

1. This case came before the District Court on stipulations of facts and exhibits filed by the parties hereto and the evidence clearly showed that CADIC was a partnership of Argentine citizens and residents; that it was organized in Argentina, having its principal and only place of business there and engaged in the business of selling in Argentina goods imported from foreign countries. It had no office in the United States at any time. It had no permanent or regular representative here. One of its partners did come here in 1947 to obtain quotations to be forwarded to the home office and to look at goods that suppliers were shipping, and, generally, to expedite shipments. While here, he was a transient, staying at a hotel; using in effect a public stenographer to write some letters; using the telephone to contact suppliers and his home office; occasionally using a supplier's clerk to make up invoices; and collecting monies made available in New York banks by the Argentine purchaser for payment to CADIC, the Argentine seller. In essence, he came to see what was being offered and what the prices were. As it was put by this Court in *Deputy* v. *Dupont*, 308 U. S. 488, at page 499:

> "Carrying on any trade or business * * * involves holding oneself out to others as engaged in the selling of goods or services."

CADIC's customers were not in the United States. CADIC did not hold itself out as prepared to sell goods or services to anyone in the United States. It was merely buying its supplies here.

On these facts the District Court held that CADIC was not engaged in trade or business in the United States (Pets.' App. 13).

When the case reached the Court of Appeals, that Court, unquestionably influenced by the Government's strategy of constant repetitions and distortions of immaterial facts and of allegations not in the record, found it necessary to get away from this holding as the District Court's decision on the taxability of the discounts was clearly erroneous. To this end it made findings either entirely unsupported in the record or inferentially based on remarks taken out of context. The principal erroneous findings, first advanced in the Government's Brief in the Court below and again intertwined strategically in the Brief in Opposition before this Court, are as follows:

> "While here, he (Balanovski) made extensive * * * sales of trucks and other equipment" (Petition, App. B, 5a).

The record is entirely devoid of any such evidence.

> "Balanovski's activities * * * required the exercise of initiative, judgment, and executive responsibility. They far transcended the routine or merely clerical" (Petition, App. B, 7a).

There is no such testimony in the record; nor is there any reasonable inference of the same, since approximately 50% of the petitioners' purchasing was done through an agent without assistance of any kind from Balanovski (Pets.' App. 50-51, Stip. pars. 35, 36).

> "Thus he conferred and bargained with American bankers" (Petition, App. B, 7a).

Obviously untrue. Letters of credit were arranged by the issuing bank in Buenos Aires; there was nothing for Balanovski to bargain for in New York. The correction of routine errors in letters of credit is a task daily handled by bank clerks (Pets.' App. 82-83).

> "And while here he attempted to develop other business for Cadic" (Petition, App. B, 7a).

A distortion of his testimony in which he obviously was referring to purchases (Gov. App. 38a).

> "Throughout his stay in the United States Balonovski employed a Miss Alice Devine as a secretary. She used, and he used, the Hotel New Weston in New York City as an office. His supplier contacted him there, and that was the place where his letters were typed and his business appointments arranged and kept. Later Miss Devine opened an office on Rector Street in New York City, which he also used" (Petition, App. B, 7a-8a).

A distortion—Miss Devine performed perfunctory duties as public stenographer and clerk; any other conclusion is unwarranted (Gov. App. 59a). The room at the Weston was not an office (Pets.' App. 71-78).

> "This (power of attorney) gave her wide latitude in arranging for shipment of goods and in signing his name to all sorts of documents, including checks. When he left for Argentina again * * * she used (it) to arrange for and complete the shipment of goods * * *" (Petition, App. B, 8a).

> "The power of attorney * * * was broad and sweeping in its terms * * *" (Petition, App. B, 11a).

The emphasis placed upon this customary bank power—limited to dealing with specific banks—well represents the Government's efforts (so far successful) in distorting the actual situation. See the exact provisions of the power (Pets.' App. 52-56).

> "CADIC was actively and extensively engaged in business in the United States in 1947. Its 80 per cent partner, Balanovski, under whose hat 80 per cent of the business may be thought to reside, was in this country soliciting orders, inspecting merchandise, making purchases, and (as will later appear) completing sales. While maintaining regular contact with his home office, he was obviously making important business decisions" (Petition, App. B, 12a).

Except for the inspection of merchandise and its acquisition, these allegations are not supported by the record and are simply untrue. This Court need not be told that if contracts were made, the place where the real work was done was Argentina.

> "Acting for CADIC he engaged in numerous transactions herein he both purchased and sold goods in this country, earned his profits here, and participated in other activities pertaining to the transaction of business" (Petition, App. B, 12a).

Except as to purchasing, there is not a single word of evidence, nor a reasonable inference therefrom, to justify the above conclusions.

> "• • • these profits flowed from transactions engineered in major part within the United States • • •" (Petition, App. B, 17a).

Obviously the profits stemmed from the sales made in Argentina.

Stripped of these fantastic claims, of which there is absolutely no proof, we have the simple situation of a non-resident alien partnership purchasing goods in the United States, which it had previously sold in Argentina, with the payment therefor occurring here incidentally through the use of letters of credit. See *Com.* v. *East Coast Oil Co.*, 85 F. 2d 322, 323. Such activity has never amounted to the statutory engaging in business.

Since this Court unquestionably has been misled by the unsupported findings of the Court of Appeals, aided and abetted by the emphasis placed therein by the Government in its Brief in Opposition, it should review the record herein.

In times like these, when the Executive Branch of the Government is intent upon creating good-will among the nations of the world, and particularly our loyal neighbors to the South, there should be no suspicion of a gross miscarriage of justice to an alien who has come here, in good faith, to purchase goods for resale at a time when the prevailing laws clearly exempted the transactions from our income tax laws. Plainly the exercise of the supervisory powers of this Court is warranted herein.

2. Another question of widespread importance in the law of taxation of non-resident aliens, as well as of Western Hemisphere trading corporations, is presented. This question may be phrased: In a letter of credit situation, does title pass to a foreign buyer upon delivery of warehouse receipts and shipping documents to the correspondent bank (N. Y.) or upon delivery of the shipping documents to the foreign buyer when he reimburses the issuing bank (B. A.) for the amount of the letter of credit?

The Court of Appeals concluded that title passed in the United States on the theory that the usual presumptions in the law of sales were not altered by the use of a letter of

credit (Petition, App. B, 15a). In so holding, the Court ignores the fact that the determinative issue (the second proposition of the Preliminary Statement above) was not the *situs* of the passage of title *from* the seller but was the place where *title passed to the buyer.*

The letter of credit and the sales contract are two distinct and independent instruments. The sales contract is an agreement between the buyer and the seller while the letter of credit is a contract between the issuing bank and the seller. "Their terms and conditions must be judged by the expressions used in each of them." *Finkelstein: Legal Aspects of Commercial Letters of Credit* (1930), p. 223; *American Steel Co.* v. *Irving National Bank,* 266 Fed. 41 (2 Cir. 1920), 277 Fed. 1016 (2 Cir. 1921), *cert. den.* 258 U. S. 617 (1922); *O'Meara Co.* v. *National Park Bank of New York,* 239 N. Y. 386 (1925).

Under the terms of the letter of credit, CADIC or its assignee was to receive payment upon delivery of the documents of title to the correspondent bank in New York. By doing so, full legal title was transferred to the New York bank. *New York Personal Property Law,* §115. Upon the transmission of these documents to the issuing bank, title is transferred to that bank in Argentina. *Gass* v. *Astoria Veneer Mills,* 121 A. D. 182, 105 N. Y. S. 794 (2nd Dept. 1907).

It has never been held, however, that the foreign purchaser acquires legal title at the time the seller delivers documents of title to the correspondent bank. The weight of authority is, rather, that title remains with the banks until the buyer takes possession of the goods and pays the purchase price. *Vaughan* v. *Massachusetts Hide Corp.,* 209 Fed. 667 (D. C. Mass. 1913); *Moors* v. *Kidder,* 106 N. Y. 33 (1887); *McCurdy, Commercial Letters of Credit,* 35 Harvard Law Review 715, 737 (1922), citing other authorities.

None of the cases cited by the Court (Petition, App. B, 15a) is comparable to a sale under the letter of credit utilized here. Under the cited cases, the foreign purchaser did not acquire title to the goods within the United States but instead received title when it received delivery and paid the purchase price in Argentina. The question presented is one of large practical importance in dealing with purchasing activities of foreigners and of Western Hemisphere trading corporations.

3. This Court has ever been zealous in protecting the rights of the oppressed. Compare *U. S.* v. *Taylor, cert. granted* January 14, 1957. Surely it need not be reminded of its very own time-worn axiom—"the power to tax is the power to destroy". Certainly it ought to satisfy itself here where a non-resident alien, in the United States to purchase goods, finds himself subject to over seven million dollars in income taxes on purchases simply because an administrative officer changes his interpretation of a statute after the alien has concluded his transactions and departed these shores.

Conclusion.

For the reasons set forth above and in the petition for writ of certiorari, it is respectfully urged that rehearing be granted and that, upon such rehearing, a writ of certiorari issue to the Court of Appeals for the Second Circuit.

Respectfully submitted,

DONALD L. STUMPF,
Counsel for Petitioners.

HÄNDEL & STUMPF,
Of Counsel.

Certificate of Counsel.

I hereby certify that the foregoing petition for rehearing is presented in good faith and not for delay and is restricted to grounds specified in Rule 58 of the rules of this Court.

DONALD L. STUMPF,
Counsel for Petitioners.